

TROLLING FOR A SOLUTION: ENDING ABUSIVE PATENT DEMAND LETTERS

HEARING BEFORE THE SUBCOMMITTEE ON COMMERCE, MANUFACTURING, AND TRADE OF THE COMMITTEE ON ENERGY AND COMMERCE HOUSE OF REPRESENTATIVES ONE HUNDRED THIRTEENTH CONGRESS

SECOND SESSION

APRIL 8, 2014

Serial No. 113-138



Printed for the use of the Committee on Energy and Commerce
energycommerce.house.gov

U.S. GOVERNMENT PUBLISHING OFFICE

90-884

WASHINGTON : 2015

For sale by the Superintendent of Documents, U.S. Government Publishing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512-1800; DC area (202) 512-1800
Fax: (202) 512-2104 Mail: Stop IDCC, Washington, DC 20402-0001

COMMITTEE ON ENERGY AND COMMERCE

FRED UPTON, Michigan
Chairman

RALPH M. HALL, Texas
JOE BARTON, Texas
Chairman Emeritus
ED WHITFIELD, Kentucky
JOHN SHIMKUS, Illinois
JOSEPH R. PITTS, Pennsylvania
GREG WALDEN, Oregon
LEE TERRY, Nebraska
MIKE ROGERS, Michigan
TIM MURPHY, Pennsylvania
MICHAEL C. BURGESS, Texas
MARSHA BLACKBURN, Tennessee
Vice Chairman
PHIL GINGREY, Georgia
STEVE SCALISE, Louisiana
ROBERT E. LATTA, Ohio
CATHY McMORRIS RODGERS, Washington
GREGG HARPER, Mississippi
LEONARD LANCE, New Jersey
BILL CASSIDY, Louisiana
BRETT GUTHRIE, Kentucky
PETE OLSON, Texas
DAVID B. MCKINLEY, West Virginia
CORY GARDNER, Colorado
MIKE POMPEO, Kansas
ADAM KINZINGER, Illinois
H. MORGAN GRIFFITH, Virginia
GUS M. BILIRAKIS, Florida
BILL JOHNSON, Missouri
BILLY LONG, Missouri
RENEE L. ELLMERS, North Carolina

HENRY A. WAXMAN, California
Ranking Member
JOHN D. DINGELL, Michigan
Chairman Emeritus
FRANK PALLONE, JR., New Jersey
BOBBY L. RUSH, Illinois
ANNA G. ESHOO, California
ELIOT L. ENGEL, New York
GENE GREEN, Texas
DIANA DeGETTE, Colorado
LOIS CAPPS, California
MICHAEL F. DOYLE, Pennsylvania
JANICE D. SCHAKOWSKY, Illinois
JIM MATHESON, Utah
G.K. BUTTERFIELD, North Carolina
JOHN BARROW, Georgia
DORIS O. MATSUI, California
DONNA M. CHRISTENSEN, Virgin Islands
KATHY CASTOR, Florida
JOHN P. SARBANES, Maryland
JERRY McNERNEY, California
BRUCE L. BRALEY, Iowa
PETER WELCH, Vermont
BEN RAY LUJAN, New Mexico
PAUL TONKO, New York
JOHN A. YARMUTH, Kentucky7

SUBCOMMITTEE ON COMMERCE, MANUFACTURING, AND TRADE

LEE TERRY, Nebraska
Chairman

LEONARD LANCE, New Jersey
Vice Chairman
MARSHA BLACKBURN, Tennessee
GREGG HARPER, Mississippi
BRETT GUTHRIE, Kentucky
PETE OLSON, Texas
DAVE B. MCKINLEY, West Virginia
MIKE POMPEO, Kansas
ADAM KINZINGER, Illinois
GUS M. BILIRAKIS, Florida
BILL JOHNSON, Missouri
BILLY LONG, Missouri
JOE BARTON, Texas
FRED UPTON, Michigan, *ex officio*

JANICE D. SCHAKOWSKY, Illinois
Ranking Member
JOHN P. SARBANES, Maryland
JERRY McNERNEY, California
PETER WELCH, Vermont
JOHN A. YARMUTH, Kentucky
JOHN D. DINGELL, Michigan
BOBBY L. RUSH, Illinois
JIM MATHESON, Utah
JOHN BARROW, Georgia
DONNA M. CHRISTENSEN, Virgin Islands
HENRY A. WAXMAN, California, *ex officio*

CONTENTS

	Page
Hon. Lee Terry, a Representative in Congress from the State of Nebraska, opening statement	1
Prepared statement	2
Hon. Janice D. Schakowsky, a Representative in Congress from the State of Illinois, opening statement	
Hon. Jerry McNerney, a Representative in Congress from the State of Cali- fornia, opening statement	5
WITNESSES	
William Sorrell, Attorney General, State of Vermont	6
Prepared statement	9
Answers to submitted questions	103
Rheo Brouillard, President and CEO, Savings Institute Bank and Trust Com- pany, on Behalf of American Bankers Association	27
Prepared statement	29
Answers to submitted questions	111
Dennis Skarvan, Deputy General Counsel, Intellectual Property Group, on Behalf of Coalition for 21st Century Patent Reform	35
Prepared statement	37
Answers to submitted questions	114
Jason Schultz, Associate Professor of Clinical Law, New York University School of Law	48
Prepared statement	50
Answers to submitted questions	130
Mark Chandler, Senior Vice President and Chief Compliance Officer, Cisco Systems Incorporated	54
Prepared statement	56
Answers to submitted questions	137
Michael Dixon, Ph.D., President and CEO, UNeMed Corporation	69
Prepared statement	71
Answers to submitted questions	142
SUBMITTED MATERIAL	
Material submitted by Mr. Terry	92

TROLLING FOR A SOLUTION: ENDING ABUSIVE PATENT DEMAND LETTERS

APRIL 8, 2014

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COMMERCE, MANUFACTURING, AND
TRADE,
COMMITTEE ON ENERGY AND COMMERCE,
Washington, DC.

The subcommittee met, pursuant to call, at 10:05 a.m., in room 2123 of the Rayburn House Office Building, Hon. Lee Terry (chairman of the subcommittee) presiding.

Members present: Representatives Terry, Lance, Olson, McKinley, Kinzinger, Bilirakis, Johnson, Long, Schakowsky, McNerney, Welch, Rush, Matheson, and Barrow.

Staff present: Charlotte Baker, Deputy Communications Director; Kirby Howard, Legislative Clerk; Brian McCullough, Senior Professional Staff Member, CMT; Paul Nagle, Chief Counsel, CMT; Shannon Weinberg Taylor, Counsel, CMT; Graham Dufault, CMT; Michelle Ash, Democratic Chief Counsel; and Will Wallace, Democratic Professional Staff Member.

Mr. TERRY. We are going to go ahead and start, and I want to thank our witnesses. This is Paul's first time in the chair replacing Gib Mullen, so, Paul, thank you for your good work. I just want to let people know, or the witnesses, I appreciate you coming here today, and one of them, extraordinary circumstances, Mr. Brouillard, who actually could have attended the NCAA final game last night, and is a UConn fan, and from Connecticut. So that is a bigger sacrifice than we usually encounter here.

Mr. BROUILLARD. I gave my tickets up to be here, Mr. Chairman.

Mr. TERRY. Yes. Now some of us are doubting your ability to make good decisions. But we are thankful that you did that. And I will introduce all of you before we actually start your testimony, and so now I am going to start my opening statement.

OPENING STATEMENT OF HON. LEE TERRY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEBRASKA

Mr. TERRY. Good morning, and welcome, everyone, to today's hearing, called, "Trolling for a Solution, Ending Abusive Patent Demand Letters". As Thomas Edison once said, to invent you need a good imagination and a pile of junk. That may be true, but I would also add that you also need to fight for your invention because, as Thomas Moore said, it is naturally given to all men to esteem their own inventions best.

Now, in competition of ideas, whether we are talking about a multinational company that spends \$8 million per day on R and D, or an inventor with a workshop in his basement, the Constitution treats intellectual property equally. So let me start by saying that we must respect the arrangement small inventors need in order to enforce their patent rights. And while we are at it, let us emphasize that not all patent assertion entities are trolls. The role of patent assertion entities is very important for small inventors who lack the resources to enforce his or her own property rights. Taking away or degrading the flexibility to assign enforcement rights would do nothing less than encroach on an inventor's constitutional right to exclude others from infringing their property rights.

With that said, what we address today are instances where bad actors extort money from innocent parties under the pretense of asserting intellectual property rights. This kind of activity belongs in the same family as other type of unfair and deceptive trade practices. Our job is to separate it from legitimate right assertions. In order to do so, we have here today a diverse panel of witnesses whose testimony gives us a variety of perspectives on the issue.

Already we are seeing a set of potentially conflicting considerations. First, patent enforcement differs across industries. According to UNeMed testimony, it considers listing patent claims and demand letters to be standard procedure. Caterpillar, on the other hand, would find it difficult in some situations to list the exact claim at issue because it often lacks access to the potentially infringing product.

Second, some argue that we should only address letters sent to end-users of patents. Now, this may fail to address situations like the one in UNeMed's testimony, where a small inventor was slapped with an abusive demand letter just after clearing an FDA approval process. Even so, the majority of complaints on this issue appear to come from the end-users who are not versed in patent law.

I will not exhaust the issues before us today, but I want to clarify one thing. Some may say that legislative action to curb abusive demand letters would devalue intellectual property rights generally. I disagree. In fact, it remains that these bad actors are arrogantly manipulating the intellectual property system and getting away with it. Several state Attorney Generals, including John Bruning of Nebraska, have brought suits under their consumer protection statutes tools, and thus have far proven difficult to use. As a result, many states are working rapidly to update their laws.

There is something to be done here, and in order to get it right we will need the assistance of all of the stakeholders and witnesses here before us today, and I thank the witnesses for being here.

[The prepared statement of Mr. Terry follows:]

PREPARED STATEMENT OF HON. LEE TERRY

Good morning, and welcome to our hearing today titled Trolling for a Solution: Ending Abusive Patent Demand Letters.

As Thomas Edison once said, "To invent, you need a good imagination and a pile of junk."

That may be true, but I would add that you also need to fight for your invention because, as Thomas More said, "It is naturally given to all men to esteem their own inventions best."

Now, in the competition of ideas-whether we are talking about a multinational company that spends \$8 million per day on R&D or an inventor with a workshop in the basement-the Constitution treats intellectual property the same.

So let me start by saying that we must respect the arrangements small inventors need to make in order to enforce their patent rights. While we're at it, let me emphasize that not all "patent assertion entities" are "trolls."

The role of the Patent Assertion Entity (PAE) is very important for a small inventor who lacks the resources to enforce his or her own property rights. Taking away or degrading the flexibility to assign enforcement rights would do nothing less than encroach on inventors' constitutional right to exclude others from infringing their property rights.

With that said, what we address today are instances where bad actors extort money from innocent parties under the pretense of asserting intellectual property rights. This kind of activity belongs in the same family as other types of unfair and deceptive trade practices-our job is to separate it from legitimate rights assertion.

In order to do so, we have here today a diverse panel of witnesses whose testimony gives us a variety of perspectives on the issue. Already, we are seeing a set of potentially conflicting considerations. First, patent enforcement differs across industries. According to UNeMed's testimony, it considers listing patent claims in demand letters to be standard procedure. Caterpillar, on the other hand, would find it difficult in some situations to list the exact claim at issue because it often lacks access to the potentially infringing product.

Second, some argue that we should only address letters sent to end users of patents. This may fail to address situations like the one in UNeMed's testimony, where a small inventor was slapped with an abusive demand letter just after clearing an FDA approval process. Even so, the majority of complaints on this issue appear to come from end users who are not versed in patent law.

I will not exhaust the issues before us today, but I want to clarify one thing. Some may say that legislative action to curb abusive demand letters would devalue intellectual property rights generally. I disagree. The fact remains that these bad actors are arrogantly manipulating the intellectual property system-and they're getting away with it.

Several state attorneys general have brought suits under their consumer protection statutes, tools that have thus far proven difficult to use-and as a result, many states are working rapidly to update their laws.

There is something to be done here and in order to get it right we'll need the assistance of all stakeholders.

I thank the witnesses for being here today and providing their valuable insights.

Mr. TERRY. Have one minute. Does anybody want it? Hearing none, I yield back my time, and recognize the Ranking Member of our subcommittee, Ms. Schakowsky.

OPENING STATEMENT OF HON. JANICE D. SCHAKOWSKY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ILLINOIS

Ms. SCHAKOWSKY. Thank you, Mr. Chairman, for holding this important hearing on patent assertion entities, also known as patent trolls. And like you, I want to develop a solution to this growing issue, and look forward to doing so in a bipartisan manner.

Trolls assert that the patents they hold have been infringed upon, sending vague and threatening letters to hundreds, or even thousands of end-users of products, typically small businesses or entrepreneurs. Those businesses are told that they can pay the patent troll to continue using the technology. Considering the cost and resources needed to vet and fight a patent infringement claim, may small businesses choose to settle the claim by paying the troll. Others investigate and fight the claims, draining precious resources, and stunting the growth of their businesses.

It costs patent trolls virtually nothing to send patent demand letters, but it can be incredibly lucrative, and business is booming. In 2011 patent troll costs U.S. businesses an estimated \$29 billion,

and the number of defendants in patent infringement lawsuits increased about 130 percent from 2007 to 2011, according to the Government Accountability Office. At best, patent trolls are misleading. At worst, they are extortionists. This is fundamentally a fairness issue. As the subcommittee charged with protecting consumers and promising fair business practices, we must take action to reduce frivolous patent claims.

I am glad that the FTC, the Federal Trade Commission, is using its existing authority to better understand the nature of patent assertion entities, and the demand letters that they issue. I look forward to the commission's analysis, which I believe will be instructive as we decide how to curb trolling.

Nonetheless, while we wait for the FTC review, there are steps that we can, and should, take now to combat patent trolls. I believe there should be more transparency and minimum standards established for patent demand letters. There are many ideas about how to increase transparency, including proposals to require the public disclosure of egregious patent demand letters. There are also suggestions as to the minimum information that should be included in a patent demand letter, including the patent allegedly infringed, and the technology used that allegedly infringes on the patent.

However, it is vitally important that we approach this issue with the recognition that many patent infringement claims are reasonable efforts to protect intellectual property. We also need to be careful to make sure that universities, research institutions, and others that develop and hold patents, but may not develop products for sale, are not labeled as trolls. In fighting trolls, we shouldn't undermine the ability of innovators to develop and defend their patents.

While our witnesses today come at this issue from a wide variety of perspectives, it was interesting to read in their prepared testimony that each believes that this is an issue in need of attention. The details of whatever legislation this committee puts forth will be incredibly important, but the fact that our witnesses unanimously agree that we have a problem is an important start. I look forward to hearing their perspective about how legislation should be structured to make sure that patent demand letters are more fair and transparent moving forward.

Again, thank you for holding this hearing today, Mr. Chairman. I yield the remainder of my time to Mr. Welch.

Mr. WELCH. Thank you very much. I am getting the opportunity to introduce our Attorney General in Vermont, and we are very proud of Bill Sorrell for the leadership that you have provided, and also the other panelists too. This is an incredible issue, and Bill Sorrell was very responsive to a lot of the folks, that range from businesses that got these unbelievable stick-up letters, to non-profits, where these parents had raised money in the community to set up a group home for disabled kids, and next thing you know, their threadbare budget is being threatened by these letters, demanding payment for—they couldn't figure it out.

And, Bill, you worked with Jerry Tarrant and others with our legal community there. It was very responsive, and you are working with your fellow Attorney Generals. Mr. Chair, our Attorney General was the former head of the Attorney Generals. He has re-

ceived numerous awards. I am not going to bore everybody with what they are, but I will tell you they are good, and a lot of us wish we had them as well. Leader in tobacco legislation, Humane Society issues, champion for kids, taking the fight about prescription drug medication abuse, and abuse of drugs in our state. So it is great to have Bill Sorrell here, and it is great to have you on the patent troll issue, and we look forward to working together to try to deal with this. Thank you. I yield back. Thank you, Ranking Member Schakowsky.

Ms. SCHAKOWSKY. And I yield back.

Mr. TERRY. All right. Does anyone on the Republican side want time? I have to talk slow to draw this out. Anybody want to talk about the game? All right. Seeing none, no one taking our time, then, Mr. McNerney, you are our resident patent holder. Would you like the minority's time?

Mr. MCNERNEY. I sure would.

Mr. TERRY. But you are the only one. You are the expert.

Mr. MCNERNEY. I thank you, Mr. Chairman.

Mr. TERRY. You are recognized for 5 minutes.

OPENING STATEMENT OF HON. JERRY MCNERNEY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Mr. MCNERNEY. I appreciate your calling this hearing. You know, if you hang around here for long enough, you see the advertisements in the Hill rags about patent trolls taking more and more money over time, and those will get your attention. If you take the Metro, you see, every so often at the Metro stops, big advertisements, so this is clearly an issue. The fact that the so-called patent trolls are demanding stick-up letters, as my friend from Vermont said, it is an issue. We need to address it. There is a general understanding that this is a problem, and I am glad to see this come up in a hearing so that we can hear your inputs, how we can move forward together, how we can best address this issue.

As the Chairman said, I have patents. One of them is a Fat Wire patent, and the other a software patent, so I kind of understand where we could be with this issue. I understand, as a small patent holder, how difficult it would be to assert your rights against a large corporation, if that comes to that.

So there is a place for patent assertion entities. I want to see that preserved, but we want to see that the sort of stick-up nature of this is curtailed, so it is a balance. It is important to have a well thought out and meaningful bipartisan discussion, and I think, on this particular issue, we have a good desire to work on a bipartisan basis.

So we have an opportunity to make it better, and I am hoping to be a part of that. I am hoping that your testimony can help guide us on the decisions that we need to make. So, with that, I am going to yield back, Mr. Chairman.

Mr. TERRY. Anyone else? All right. So Mr. Schultz—

Ms. SCHAKOWSKY. Would either of the other members of the committee—no? OK. Mr. Matheson or Mr. Barrow? No? OK. Thank you.

Mr. TERRY. Gentlelady yields back, and so I want to introduce our panel now. Bill Sorrell is one of our resident expert witnesses from the AG's office, and we appreciate you being here today. For those of you who haven't testified before us, we go stage left to right, so, Mr. Sorrell, as Attorney General of Vermont, will go first.

Then we now have Mr. Bouillard, the person who gave up his tickets last night to be here, and your sacrifice is massive, and well appreciated. You represent the Savings Institute Bank and Trust Company on behalf of the American Bankers Association. Then, next to him, Mr. Skarvan is Deputy General Counsel, Intellectual Property for Caterpillar. Appreciate your appearance.

Then Mr. Schultz, or as we call him, Jason "Just In Time" Schultz, Associate Professor of Clinical Law, New York University School of Law, and we understand it has been a difficult morning for you, and we appreciate that you undertook these heroic efforts to get here today. Thank you.

Then we have Mr. Mark Chandler, Senior Vice President and Chief Compliance Officer of Cisco Systems, who has great experience with these type of demand letters.

Then, last, Mr. Michael Dixon, Ph.D. Dr. Dixon is President and CEO of UNeMed Corporation, University of Nebraska's holding business of all of the patents generated by the University.

So, at this time, Mr. Sorrell, you are recognized for your 5 minutes.

STATEMENTS OF THE HONORABLE WILLIAM SORRELL, ATTORNEY GENERAL, STATE OF VERMONT; RHEO BROUILLARD, PRESIDENT AND CEO, SAVINGS INSTITUTE BANK AND TRUST COMPANY, ON BEHALF OF AMERICAN BANKERS ASSOCIATION; DENNIS SKARVAN, DEPUTY GENERAL COUNSEL, INTELLECTUAL PROPERTY GROUP, ON BEHALF OF COALITION FOR 21ST CENTURY PATENT REFORM; JASON SCHULTZ, ASSOCIATE PROFESSOR OF CLINICAL LAW, NEW YORK UNIVERSITY SCHOOL OF LAW; MARK CHANDLER, SENIOR VICE PRESIDENT AND CHIEF COMPLIANCE OFFICER, CISCO SYSTEMS INCORPORATED; AND MICHAEL DIXON, PH.D., PRESIDENT AND CEO, UNEMED CORPORATION

STATEMENT OF WILLIAM SORRELL

Mr. SORRELL. Thank you, Mr. Chairman, Ranking Member Schakowsky, members of the subcommittee. Thank you much for the opportunity to appear today and speak about an issue that is of great importance to the Nation's Attorneys General, as evidenced by the fact that 42 offices signed on to a sign-on letter that we sent to the Senate drafted by General Buling and myself in February on these issues. Much of the work in the House and in the Senate on assertions of patent infringement have related to abusive litigation tactics, but the truth of the matter is that is just the tip of the iceberg, and I want to talk some today about the iceberg, the roughly as much as 99 percent of cases that don't result in the filing of a civil complaint.

And so I want to talk about, for example, Lincoln Street, Inc., a small nonprofit in Springfield, Vermont with 16 direct care workers, 12 or 13 administration and support staff, that provide home

care to developmentally disabled Vermonters. In the fall of 2012, Lincoln Street received a letter from one of the roughly 40 shell subsidiary corporations of a parent corporation by the name of MPHJ Technology Investments, LLC. Paraphrasing, the letter says, we own patents X and Y, we believe you are in violation of them, and that you are scanning documents and sending those in e-mail through a computer network. Please be in touch with us within 2 weeks and prove to us that you are not infringing our patent, or talk to us about resolving this, and paying licensing fees to us. We have had a very positive response around the country from the business community, many companies agreeing to pay us \$1,000 per employee.

A couple weeks later, a second letter comes, this time from a Texas law firm by the name of Farney Daniels says, we have been retained because you didn't respond to the first letter. This is serious. We hope that we don't have to get to litigation, but unless you are in touch with us forthwith and resolve this amicably, it is going to be trouble, please take this serious. And then there is the third letter a couple weeks later, also from Farney Daniels. This one attaches a draft, Federal Court Complaint, against the recipient of the letter, and says that, if you don't resolve this with us within 2 weeks, we will, "be forced to file a complaint against you." If you are not in touch with us in 2 weeks, "litigation will ensue otherwise."

Well, it wasn't just Lincoln Street that received that letter in the fall of 2012. We ultimately learned that 75 small businesses and nonprofits in the state received letters from one or other of the shell subsidiaries. And when we filed the first of its kind in the nation lawsuit in the spring of 2013 against MPHJ, as of that time, not one lawsuit had been filed in Vermont, nor had, to our knowledge, a lawsuit been filed by MPHJ, or any of its shell subsidiaries, anywhere in the country. The Federal Trade Commission, in a draft complaint against MPHJ, has looked outside Vermont, and in its draft complaint says that one of the 80 or more shell subsidiaries of MPHJ sent demand letters to 16,450 small businesses and nonprofits in all 50 states in this country.

So that is part of the iceberg. Rest of the iceberg, or other parts of the iceberg, are demand letters to smaller financial institutions saying, your ATMs use the web, they are in violation of our patent. Others go to local coffee houses that have free Wi-Fi, we have patents, you are in violation of those, please pay up.

We filed our lawsuit in State Court. We were immediately removed to Federal Court, and MPHJ has said, one, we are totally pre-empted, because this is a patent matter. You can't be enforcing your State Consumer Protection Acts against us. And, second of all, you lack personal jurisdiction over us because all we have simply done is asserted patent infringement, and that doesn't subject us to personal jurisdiction.

We also enacted in Vermont a statute on bad faith assertions of patent infringement at the request of various well known Vermont companies, and Utah, Virginia, Wisconsin, and Oregon have followed suit and adopted their own statutes. There are many others considering it. We hope that the Congress will take action, have more transparency in this arena, and evidence at the time of the

assertion of patent infringement of any other proceedings or court matters that have ruled upon the patents in question. We want express statements that the states are not pre-empted, and that we have personal jurisdiction for those that blanket our states with these assertions of patent infringement.

I have got 21 seconds left, but—sorry, I read it wrong. Thank you very much.

[The prepared statement of Mr. Sorrell follows:]

WILLIAM H. SORRELL
ATTORNEY GENERAL

SUSANNE YOUNG
DEPUTY ATTORNEY GENERAL

WILLIAM E. GRIFFIN
CHIEF ASST. ATTORNEY GENERAL



TEL: (802) 828-3171
FAX: (802) 828-2154

STATE OF VERMONT
OFFICE OF THE ATTORNEY GENERAL
109 STATE STREET
MONTPELIER
05609-1001

**Testimony of Vermont Attorney General William H. Sorrell
Before the United States House of Representatives
Committee on Energy and Commerce
Subcommittee on Commerce, Manufacturing, and Trade
April 8, 2014**

Summary

Chairman Terry, Ranking Member Schakowsky, and members of the Subcommittee, thank you for the opportunity to testify today. The issue of abusive patent demand letters is important to many of my constituents in Vermont, including small businesses, banks, credit unions, and non-profit organizations. It is also an issue of significance to me, and one that the Vermont Attorney General's Office has been actively working on for over a year.

Many Vermont businesses and non-profits have received abusive patent demand letters. For clarification, abusive demand letters, as I see them, are not straightforward allegations of infringement sent by competitors in an attempt to negotiate a reasonable license. Instead, demand letters are abusive if they, for example, are indiscriminately sent to businesses with little or no understanding of patents; are so vague as to not provide the recipient with a basic understanding of the patent, the alleged infringement, and the party with whom they are negotiating; or include misleading or untruthful statements in an attempt to influence the recipient's behavior.

This is a serious consumer protection issue. Many of these patent demands never result in litigation but they do impose real costs. The imbalance of information coupled with the aggressive and threatening tactics of some patent assertion entities leaves many businesses with few choices. The license may only be offered for a limited amount of time and the letter may threaten expensive litigation if the recipient does not pay. Small businesses and non-profits that are targeted with these letters often conclude that paying for a license is the only practical option.

My office has been actively working on ways to identify and investigate patent holders that are engaging in unfair and deceptive acts. We have taken enforcement action under the Vermont Consumer Protection Act to prevent bad actors from using unfair and deceptive tactics on Vermont businesses. Vermont's legislature has also enacted legislation designed to provide both targets of abusive demand letters and my office with additional tools.

The federal government should also take action to bolster the states' efforts to protect small businesses and non-profits. These actions should include:

- Passing legislation that requires specific disclosures to increase transparency in patent demand letters and confirms that patent holders are prohibited from engaging in unfair and deceptive practices in the enforcement of their patents.
- Confirming the authority of state law enforcement agencies to enforce consumer protection statutes, as well as other statutes, to protect constituents against abusive patent demand letters.

Dangers of Abusive Demand Letters

I have supported proposed patent litigation reform efforts and am heartened by serious work being done in Congress to address these important and complicated issues. However, litigation reform alone fails to address a large part of the abusive patent assertion problem, because it does not temper the practice of entities sending unfair and deceptive demand letters.

The limited research available confirms the experience of my office, which is that the majority of businesses receiving demand letters are never actually sued. One academic study found that of seventy-nine startup companies that reported receiving demand letters, two-thirds were never sued.¹ One estimate of the ratio of demand letters to suits actually filed is 100:1.² This disparate ratio between demand letters sent by patent assertion entities and lawsuits actually filed is illustrated by many of the more prominent patent assertion campaigns. One patent assertion entity, Innovatio IP Ventures, LLC, which claimed a patent on wi-fi technology, sent over 8,000 letters to targets around the country seeking licensing fees,³ but ultimately filed only 27 infringement lawsuits.⁴ My office has filed suit against MPHJ Technology Investments, LLC, alleging that it has violated Vermont's consumer protection statute by engaging in unfair acts and including deceptive statements in its demand letters. MPHJ sent demand letters to seventy-five Vermont businesses and non-profits in 2012 and 2013,⁵ and, to date, has not filed suit against any of them. Nationally, MPHJ has sent over 16,000 patent demand letters,⁶ and has sued just five businesses.⁷

¹ Colleen Chien, *Startups and Patent Trolls*, Santa Clare Univ. Legal Studies Research Paper No. 09-12, p.3 n.14 (Sept. 28, 2012).

² Colleen Chien, *Introduction to Patent Assertion Entity Activity*, Department of Justice, Federal Trade Commission Workshop on Patent Assertion Entity Activity, Washington, DC, (December 10, 2012), available at <http://www.justice.gov/atr/public/workshops/pae/>.

³ See *Innovatio IP Ventures, LLC Patent Litigation*, 921 F. Supp. 2d 903, 907 (N.D. Ill. 2013).

⁴ PACER search conducted on April 4, 2014 confirming that Innovatio IP Ventures, LLC was the plaintiff in 27 patent lawsuits.

⁵ See State of Vermont's Opposition to Defendant's Motion to Dismiss for Lack of Personal Jurisdiction at 4 n.1, *Vermont v. MPHJ Tech. Invs., LLC*, No. 2:13-cv-00170 (D. Vt. Nov. 17, 2013), available at <http://www.atg.state.vt.us/assets/files/MPHJ%20-%20State%20Opposition%20to%20Motion%20to%20Dismiss.pdf>.

⁶ See Complaint at ¶¶ 82, 104, *MPHJ Tech. Invs., LLC v. Federal Trade Commission*, No. 6:14-cv-11 (W.D. Tex. Jan. 13, 2014) (indicating that MPHJ sent letters to 6,000 companies with 25 to 49 employees and approximately 10,000 companies with 50 to 99 employees), available at

Specific data on the proliferation of patent demand letters is not available because, unlike lawsuits, the letters are not publicly available. This means we have limited information about both the number of demand letters sent and the response that patent holders get from recipients. However, there is clearly a volume-based model of patent enforcement that involves sending large numbers of demand letters with the aim of extracting a relatively small licensing fee from many targets. Patent assertion entities following this model often target small businesses and non-profits that do not have in-house legal counsel and have never retained patent counsel. It costs these targeted businesses thousands of dollars to retain patent counsel just to provide a simple opinion on the patent and its applicability.⁸ Moreover, if they choose to litigate, the median cost for defending claims of patent infringement by non-practicing entities⁹ ranges from \$600,000 to \$4,000,000 depending on the amount of money at risk.¹⁰ By asking for a license fee that is significant, but far less than the cost of even successful litigation, there is a strong incentive for less sophisticated companies to pay for the license. For example, MPHJ, the patent assertion entity that we have sued, asked for license fees ranging from \$900 to \$1200 per

<http://ia600804.us.archive.org/28/items/gov.uscourts.txwd.669787/gov.uscourts.txwd.669787.1.0.pdf> (hereinafter “MPHJ-FTC Complaint”).

⁷ See *MPHJ Tech. Invs., LLC v. Dillard’s Inc.*, No. 1:14-cv-00004 (D. Del. filed Jan. 1, 2014); *MPHJ Tech. Invs., LLC v. Unum Group*, No. 1:14-cv-00006 (D. Del. filed Jan. 3, 2014); *MPHJ Tech. Invs., LLC v. Coca-Cola Company*, No. 1:14-cv-00003 (D. Del. filed Jan. 3, 2014); *MPHJ Tech. Invs., LLC v. Huhtamaki Americas Inc.*, No. 1:14-cv-00005 (D. Del. filed Jan. 3, 2014); *MPHJ Tech. Invs., LLC v. Research Now, Inc.*, No. 2:13-cv-00962 (E.D. Tex. filed Nov. 19, 2013).

⁸ See American Intellectual Property Law Association, *Report of the Economic Survey 2013* at 27 (2013) (noting that the median charge for a “combination validity and infringement per patent” in 2012 was approximately \$15,000).

⁹ A non-practicing entity primarily makes money based on the licensing and enforcement of its patents rather than the making or selling of products or services.

¹⁰ See *id.* at 35.

employee.¹¹ For many of the very small businesses targeted by MPHJ, the cost of a license would have been less than consulting with a patent attorney.

Given the significant cost of litigation, the story often ends with the demand letter. This is why it is important to assure that demand letters are transparent, understandable, and truthful. In my experience, this is often not the case. It is not uncommon for such letters to:

- be sent with little or no investigation to determine whether the recipient is or could be infringing the relevant patents;
- provide very limited information regarding the relevant patents;
- be sent from shell corporations, requiring the recipient to track down the true owner of the patent;
- threaten imminent litigation if a licensing fee is not paid;
- be sent without the intention of filing litigation;
- warn recipients of the significant costs associated with litigation if the recipient does not purchase a license;
- be targeted to smaller businesses that are less likely to have the resources or legal staff to fight back; and
- be sent to the end-users of technology rather than the manufacturer of the product that is giving rise to the alleged infringement.

For example, in the case of MPHJ, the demand letters sent to Vermont businesses were sent from forty different shell corporations that were wholly owned subsidiaries of MPHJ.¹² The Federal Trade Commission (“FTC”), in a draft complaint that it provided to MPHJ, alleged that there were over eighty subsidiaries of MPHJ sending letters nationwide.¹³ The use of shell

¹¹ See Consumer Protection Complaint at ¶ 23, *Vermont v. MPHJ Tech. Invs., LLC*, No. 282-5-13Wnc (Vt. Super. Ct. May 8, 2013), available at <http://www.atg.state.vt.us/assets/files/MPHJ%20-%20Complaint.pdf>.

¹² *Id.* at ¶ 3.

¹³ The FTC’s draft complaint was made public in a lawsuit filed by MPHJ against the FTC. See *MPHJ-FTC Complaint* at Exhibit F, available at https://www.eff.org/files/2014/01/14/draft_ftc_compl_to_mphj.pdf.

corporations makes it difficult for unsophisticated small businesses to identify the real owner of the patent, and it makes it more challenging for recipients of such demand letters to locate and communicate with others who have been targeted. Another example of the lack of transparency in demand letters can be seen in letters sent by Automated Transactions, LLC. Some publicly available examples of these letters provide almost no explanation of the scope of the patent or its claims, leaving recipients without a basis for evaluating whether it is infringing.¹⁴

Patent reform that fails to address the proliferation of abusive demand letters only addresses a fraction of the problem. Because businesses face substantial financial risks associated with litigation, much of the activity around patent enforcement happens before court. For this reason, it is essential that the federal government and the states take action to assure that these pre-litigation transactions are taking place in an honest and fair way with sufficient transparency for businesses to make reasonable and informed decisions.

State Efforts to Address Abusive Demand Letters

States have been grappling with the problem of abusive patent demand letters. As I discussed earlier, my office is currently engaged in litigation with MPHJ, which is a patent assertion entity that we believe engaged in unfair and deceptive acts to convince small businesses and non-profits in Vermont to pay licensing fees. Other states, including Nebraska, Minnesota, and New York have also investigated MPHJ. New York has entered into a settlement with MPHJ intended to increase the transparency in their patent demand letters.¹⁵ Many other states are

¹⁴ See *Protecting Small Businesses and Promoting Innovation by Limiting Patent Troll Abuse Before Senate Committee on the Judiciary*, 113th Cong. (2013) (Statement for the Record on Behalf of the American Bankers Association), available at <http://www.aba.com/Advocacy/LetterstoCongress/Documents/PatentTrolls-SJUDStatementforRecord-121713.pdf>.

¹⁵ See Assurance of Discontinuance, No. 14-015 (Jan. 13, 2014), available at <http://www.ag.ny.gov/pdfs/FINALAODMPHJ.pdf>.

similarly investigating the possibility of unfair and deceptive activities by other patent assertion entities.

Additionally, Vermont passed legislation almost a year ago that took a number of steps to curb the activity of patent assertion entities sending demand letters in bad faith to Vermont businesses and non-profits. The law, as passed, is Exhibit A to my testimony. This law prohibits bad faith assertions of patent infringement, and it identifies a number of factors as evidencing bad faith, including the absence of a patent number and the name and address of the patent holder in the letter; failing to compare the patent's claims to the target's products, services, or technology; and demanding a license fee in an unreasonably short period of time. The legislation provides for enforcement authority by the Attorney General as well as a private right of action that empowers recipients of bad faith patent assertions to move forward themselves.¹⁶ A number of other states are considering comparable legislation,¹⁷ and Oregon,¹⁸ Utah,¹⁹ Wisconsin,²⁰ and Virginia²¹ have passed similar legislation this year in an attempt to begin addressing the issue of abusive patent demand letters.

¹⁶ See 9 V.S.A. §§ 4195-99, available at <http://www.leg.state.vt.us/statutes/sections.cfm?Title=09&Chapter=120>.

¹⁷ See, e.g., S.B. 116, Reg. Sess. (Ky. 2014) (passed Senate and pending in the House), available at <http://www.irc.ky.gov/record/14RS/SB116.htm>; H.B. 1374, 97th Gen. Assemb., 2nd Reg. Sess. (Mo. 2014) (passed House and pending in Senate), available at <http://www.house.mo.gov/BillActions.aspx?bill=HB1374&year=2014&code=R>.

¹⁸ See S.B. 1540, 77th Leg., Reg. Sess. (Or. 2014), available at <https://olis.leg.state.or.us/liz/2014R1/Measures/Overview/SB1540>.

¹⁹ See H.B. 117, Gen. Sess. (Utah 2014), available at <http://le.utah.gov/~2014/bills/static/HB0117.html>.

²⁰ See S.B. 498, 2013-2014 Leg., Reg. Sess. (Wis. 2014) (the Wisconsin legislature has passed the bill, but it has not been signed by the governor), available at <http://docs.legis.wisconsin.gov/2013/related/proposals/sb498>.

²¹ See S.B. 150, 2014 Sess. (Va. 2014) (the Virginia legislature has passed the bill, but it has not been signed by the governor), available at <http://leg1.state.va.us/cgi-bin/legp504.exe?141+cab+SC10129SB0150+UCSB2>.

Even as the states take efforts both through enforcement action and through legislation to address abusive patent demand letters, my office continues to field complaints from small businesses that are being targeted by predatory patent assertion practices. These businesses often lack the resources to effectively fight a patent challenge and are unable to evaluate an appropriate course of action based on the information in the letters that they receive. It is in this context, where a large number of small businesses and non-profits are being targeted by unfair and deceptive practices, that states and the FTC can effectively protect the public.

Our experience litigating against MPHJ illustrates why congressional action would help state and federal regulators do their jobs better. Eleven months after Vermont filed its consumer protection action against MPHJ, we have had no discovery and no proceedings on the merits. MPHJ removed the case to federal court, even though Vermont sued solely under state law; they have argued that Vermont courts do not have personal jurisdiction over MPHJ; and they have continually insisted that the entire case is preempted by federal law. We are waiting for the federal district court to rule on these issues. And MPHJ has fought the FTC's regulation as well. MPHJ sued the FTC after learning of its investigation. They claim that the FTC has no statutory authority to police their conduct. I believe that MPHJ's understanding of personal jurisdiction, preemption, and the scope of state and federal authority to enforce consumer protection statutes is mistaken. But federal legislation clarifying these issues and confirming state authority would make it far easier for states and the FTC to curb these abusive practices.

First, Congressional confirmation of personal jurisdiction would be valuable in facilitating appropriate enforcement action by the states. Patent assertion entities typically argue that they cannot be sued in the states where they targeted businesses with demand letters. Despite acknowledging that the constitutional requirement of "minimum contacts" is satisfied, the

Federal Circuit, which hears all patent appeals, has found that the courts in the state where a recipient received a patent demand letter do not have personal jurisdiction to hear a declaratory judgment action against the patent holder to decide the validity or scope of the patent.²² The Federal Circuit has concluded that there are “policy considerations unique to the patent context”²³ that limit personal jurisdiction in these cases. Congress can and should confirm that the Federal Circuit’s reasoning in these cases has no relevance to consumer protection actions and that a state has personal jurisdiction to enforce its laws against patent holders that send demand letters into the state.

Congress can also support states’ efforts to deal with this difficult issue by confirming that state-law claims that demand letters are unfair or deceptive are not preempted by federal patent law. MPHJ, for example, has argued that any enforcement action under state law relating to the content of patent demand letters is preempted by federal patent law unless Vermont can prove that the patent was either invalid or objectively not infringed.²⁴ This position fails to address the rampant problem of patent assertion entities sending vague and misleading letters to businesses and non-profits that they know little or nothing about. In these instances, the validity of the patent is not the point; it is the letters that are problematic and unfair. It is nonsensical to think that patent law preempts claims that are unrelated to the patent itself, but instead seek to address the unfair and deceptive acts of the patent holder.

²² *Silent Drive, Inc. v. Strong Indus., Inc.*, 326 F.3d 1194, 1206 (Fed. Cir. 2003).

²³ *Id.*

²⁴ See MPHJ Technology Investments, LLC’s Memorandum in Support of its Motion for Sanctions Under Rule 11, 28 U.S.C. § 1927, and the Court’s Inherent Authority at 16, 19, *Vermont v. MPHJ Tech. Invs., LLC*, 2:13-cv-00170 (D. Vt. Feb. 7, 2014).

Recommendations for Federal Action

The states are actively utilizing the tools available to them to combat a problem that unnecessarily disrupts and interferes with the everyday activities of businesses. There are a number of actions that the federal government can take to both affirmatively protect businesses and non-profits from predatory and abusive demand letters and assist states in their ongoing efforts.

Requiring specific disclosures to increase transparency and confirming the prohibition on unfair and deceptive acts in patent demand letters. This Subcommittee has recognized the need to distinguish between “bad actors” and those “entities with significant patent holdings [that] use demand letters to engage other companies in lawful and productive discussions around their businesses.”²⁵ This distinction is important. It is the unfair and abusive actions of certain patent assertion entities that distinguishes them from legitimate patent holders attempting to negotiate fair and reasonable licenses for their inventions. Part of the solution is transparency. Congress should be specifying that certain information must be provided in patent demand letters, such as: patent numbers, descriptions of the patents, owners of the patents, the relevant claims of the patents, pending or completed administrative or judicial proceedings regarding the patents, and an explanation of how the recipient’s product or service allegedly infringes the patents. Failing to include this information makes patent demand letters misleading and it limits the ability of the recipient to reasonably evaluate the asserted infringement.

In addition to requiring transparency, patent holders should be held accountable for making unfair and deceptive statements in their letters. For example, they should not be allowed

²⁵ *Trolling for a Solution: Ending Abusive Patent Demand Letters: Hearing Before the H. Subcomm. on Commerce, Manufacturing, and Trade, 113th Cong. (April 8, 2014), available at <http://energycommerce.house.gov/press-release/hearing-notice-subcommittee-commerce-manufacturing-and-trade>.*

to threaten lawsuits that they are neither able nor intending to file, to inaccurately or inadequately describe the response that they have gotten from other businesses, or to provide an unreasonably short time to pay for a license. Congress should confirm both that such activities are unfair and deceptive and that the FTC and states have authority to protect businesses against such practices. By both increasing transparency and confirming that patent holders do not have a pass to engage in unfair and deceptive acts, Congress will allow recipients of demand letters to more fully evaluate their options and allow the FTC and states to prevent unfair and deceptive practices.

Congress should confirm the authority of states, under both traditional consumer protection statutes and new legislation addressing bad faith assertions of infringement, to protect businesses and non-profits targeted by entities sending abusive patent demand letters. As discussed earlier, in seeking to protect Vermont businesses from unfair and deceptive acts by patent holders, my office has faced claims that such enforcement action is preempted by federal patent law and that there is no personal jurisdiction in the State of Vermont over an entity that had offered licenses to seventy-five businesses in the state. Congressional action can confirm state authority on both points.

With respect to preemption, I ask that Congress clarify that federal patent law preempts only the subject areas in which it covers, and does not grant general immunity for patent holders to mislead and confuse recipients of patent demand letters. States are not trying to undermine the validity of patents. States are challenging activities such as sending letters indiscriminately; providing inadequate information for the recipient of a letter to evaluate whether its products or services are infringing; and including misleading information designed to intimidate the recipient of a letter into quickly taking a license. These are unfair and deceptive acts that the states are experienced at evaluating and equipped to protect against. By confirming that federal patent laws

do not preempt the enforcement of state laws that are unrelated to substantive questions of patent law, states will be able to move forward with greater confidence in addressing abusive patent demand letters.

The question of personal jurisdiction can similarly be addressed by Congress, as it is policy considerations that justify the Federal Circuit's bright line rule that sending demand letters does not give rise to personal jurisdiction over a patent action for declaratory judgment. In order for states to effectively protect local businesses, I ask that confirm that no policy considerations grounded in federal patent law prevent states from exercising jurisdiction over entities that send unfair and deceptive patent demand letters in the states.

Providing a framework to address the most egregious patent demand letters, while clarifying the authority of both the FTC and the states to take enforcement actions against the patent holders that engage in unfair and deceptive practices are both important steps that Congress can take to address the dangers of abusive demand letters.

Conclusion

The states have direct and ongoing contact with businesses and non-profits that are often the targets of abusive patent demand letters. My office, in the small state of Vermont, has received numerous calls from small businesses that have received abusive letters and are trying to determine an appropriate course of action. Acting on little information, and often without legal assistance because it is not affordable, small businesses pay thousands of dollars in licensing fees for standard products being used for their advertised purpose or live with the fear that they will be sued. It is imperative that these small businesses be provided with the basic level of information necessary to evaluate their options and to not be misled or treated unfairly while doing so. It is also necessary that both the states and the FTC have the authority to intervene to

protect these small businesses and non-profits when patent demand letters are vague, unclear, and misleading.

Thank you very much for your attention to this very important matter.

Exhibit A

The Vermont Statutes Online

Title 9: Commerce and Trade

*Chapter 120: BAD FAITH ASSERTIONS OF PATENT INFRINGEMENT***§ 4195. Legislative findings and statement of purpose**

(a) The General Assembly finds that:

(1) Vermont is striving to build an entrepreneurial and knowledge based economy. Attracting and nurturing small- and medium-size Internet technology ("IT") and other knowledge-based companies is an important part of this effort and will be beneficial to Vermont's future.

(2) Patents are essential to encouraging innovation, especially in the IT and knowledge-based fields. The protections afforded by the federal patent system create an incentive to invest in research and innovation, which spurs economic growth. Patent holders have every right to enforce their patents when they are infringed, and patent enforcement litigation is necessary to protect intellectual property.

(3) The General Assembly does not wish to interfere with the good faith enforcement of patents or good faith patent litigation. The General Assembly also recognizes that Vermont is preempted from passing any law that conflicts with federal patent law.

(4) Patent litigation can be technical, complex, and expensive. The expense of patent litigation, which may cost hundreds of thousands of dollars or more, can be a significant burden on small- and medium-size companies. Vermont wishes to help its businesses avoid these costs by encouraging the most efficient resolution of patent infringement claims without conflicting with federal law.

(5) In order for Vermont companies to be able to respond promptly and efficiently to patent infringement assertions against them, it is necessary that they receive specific information regarding how their product, service, or technology may have infringed the patent at issue. Receiving such information at an early stage will facilitate the resolution of claims and lessen the burden of potential litigation on Vermont companies.

(6) Abusive patent litigation, and especially the assertion of bad faith infringement claims, can harm Vermont companies. A business that receives a letter asserting such claims faces the threat of expensive and protracted litigation and may feel that it has no choice but to settle and to pay a licensing fee, even if the claim is meritless. This is especially so for small- and medium-

size companies and nonprofits that lack the resources to investigate and defend themselves against infringement claims.

(7) Not only do bad faith patent infringement claims impose a significant burden on individual Vermont businesses, they also undermine Vermont's efforts to attract and nurture small- and medium-size IT and other knowledge-based companies. Funds used to avoid the threat of bad faith litigation are no longer available to invest, produce new products, expand, or hire new workers, thereby harming Vermont's economy.

(b) Through this narrowly focused act, the General Assembly seeks to facilitate the efficient and prompt resolution of patent infringement claims, protect Vermont businesses from abusive and bad faith assertions of patent infringement, and build Vermont's economy, while at the same time respecting federal law and being careful to not interfere with legitimate patent enforcement actions. (Added 2013, No. 44, § 6; 2013, No. 47, § 2, eff. May 24, 2013.)

§ 4196. Definitions

In this chapter:

(1) "Demand letter" means a letter, e-mail, or other communication asserting or claiming that the target has engaged in patent infringement.

(2) "Target" means a Vermont person:

(A) who has received a demand letter or against whom an assertion or allegation of patent infringement has been made;

(B) who has been threatened with litigation or against whom a lawsuit has been filed alleging patent infringement; or

(C) whose customers have received a demand letter asserting that the person's product, service, or technology has infringed a patent. (Added 2013, No. 44, § 6; 2013, No. 47, § 2, eff. May 24, 2013.)

§ 4197. Bad faith assertions of patent infringement

(a) A person shall not make a bad faith assertion of patent infringement.

(b) A court may consider the following factors as evidence that a person has made a bad faith assertion of patent infringement:

(1) The demand letter does not contain the following information:

(A) the patent number;

(B) the name and address of the patent owner or owners and assignee or assignees, if any; and

(C) factual allegations concerning the specific areas in which the target's products, services, and technology infringe the patent or are covered by the claims in the patent.

(2) Prior to sending the demand letter, the person fails to conduct an analysis comparing the claims in the patent to the target's products, services, and technology, or such an analysis was done but does not identify specific areas in which the products, services, and technology are covered by the claims in the patent.

(3) The demand letter lacks the information described in subdivision (1) of this subsection, the target requests the information, and the person fails to provide the information within a reasonable period of time.

(4) The demand letter demands payment of a license fee or response within an unreasonably short period of time.

(5) The person offers to license the patent for an amount that is not based on a reasonable estimate of the value of the license.

(6) The claim or assertion of patent infringement is meritless, and the person knew, or should have known, that the claim or assertion is meritless.

(7) The claim or assertion of patent infringement is deceptive.

(8) The person or its subsidiaries or affiliates have previously filed or threatened to file one or more lawsuits based on the same or similar claim of patent infringement and:

(A) those threats or lawsuits lacked the information described in subdivision (1) of this subsection; or

(B) the person attempted to enforce the claim of patent infringement in litigation and a court found the claim to be meritless.

(9) Any other factor the court finds relevant.

(c) A court may consider the following factors as evidence that a person has not made a bad faith assertion of patent infringement:

(1) The demand letter contains the information described in subdivision (b)(1) of this section.

(2) Where the demand letter lacks the information described in subdivision (b)(1) of this section and the target requests the information, the person provides the information within a reasonable period of time.

(3) The person engages in a good faith effort to establish that the target has infringed the patent and to negotiate an appropriate remedy.

(4) The person makes a substantial investment in the use of the patent or in the production or sale of a product or item covered by the patent.

(5) The person is:

(A) the inventor or joint inventor of the patent or, in the case of a patent filed by and awarded to an assignee of the original inventor or joint inventor, is the original assignee; or

(B) an institution of higher education or a technology transfer organization owned or affiliated with an institution of higher education.

(6) The person has:

(A) demonstrated good faith business practices in previous efforts to enforce the patent, or a substantially similar patent; or

(B) successfully enforced the patent, or a substantially similar patent, through litigation.

(7) Any other factor the court finds relevant. (Added 2013, No. 44, § 6; 2013, No. 47, § 2, eff. May 24, 2013.)

§ 4198. Bond

Upon motion by a target and a finding by the court that a target has established a reasonable likelihood that a person has made a bad faith assertion of patent infringement in violation of this chapter, the court shall require the person to post a bond in an amount equal to a good faith estimate of the target's costs to litigate the claim and amounts reasonably likely to be recovered under subsection 4199(b) of this chapter, conditioned upon payment of any amounts finally determined to be due to the target. A hearing shall be held if either party so requests. A bond ordered pursuant to this section shall not exceed \$250,000.00. The court may waive the bond requirement if it finds the person has available assets equal to the amount of the proposed bond or for other good cause shown. (Added 2013, No. 44, § 6; 2013, No. 47, § 2, eff. May 24, 2013.)

§ 4199. Enforcement; remedies; damages

(a) The Attorney General shall have the same authority under this chapter to make rules, conduct civil investigations, bring civil actions, and enter into assurances of discontinuance as

provided under chapter 63 of this title. In an action brought by the Attorney General under this chapter, the court may award or impose any relief available under chapter 63 of this title.

(b) A target of conduct involving assertions of patent infringement, or a person aggrieved by a violation of this chapter or by a violation of rules adopted under this chapter, may bring an action in Superior Court. A court may award the following remedies to a plaintiff who prevails in an action brought pursuant to this subsection:

- (1) equitable relief;
- (2) damages;
- (3) costs and fees, including reasonable attorney's fees; and
- (4) exemplary damages in an amount equal to \$50,000.00 or three times the total of damages, costs, and fees, whichever is greater.

(c) This chapter shall not be construed to limit rights and remedies available to the State of Vermont or to any person under any other law and shall not alter or restrict the Attorney General's authority under chapter 63 of this title with regard to conduct involving assertions of patent infringement. (Added 2013, No. 44, § 6; 2013, No. 47, § 2, eff. May 24, 2013.)

Mr. TERRY. Thank you, Bill.

Mr. Brouillard, you are now recognized for your 5 minutes.

STATEMENT OF RHEO BROUILLARD

Mr. BROUILLARD. Thank you, Mr. Chairman, and Ranking Member Schakowsky. Thank you again for giving us the chance to come and present our information to you today. My bank is a \$1.3 billion community bank that has been established since 1842. We serve Connecticut, and parts of Rhode Island.

Obviously, the U.S. has a robust patent system which protects the rights of legitimate patent holders, and we believe those rights should continue to be protected. Patent trolls, however, as we have heard, abuse this system, and are serious threats to small businesses, banks, and credit unions throughout the country.

For the cost of postage, a little stationary, and some time, these trolls use unscrupulous tactics to extort licensing fees from companies too small to pay the cost to defend themselves. The claims are often intentionally vague, and based on shaky legal standing. However, when confronted with threats of expensive litigation, many banks, especially smaller ones, find that their only option is to settle, rather than paying the millions of dollars it may cost to defend against extortive claims of patent infringement.

I have seen this firsthand at my bank. In January 2013 a patent troll targeted my bank with a very vague letter, one page, claiming that they had conducted an investigation, and that our ATMs operated in a way that infringed upon their patents. Their letter included an exhibit which listed 13 patent numbers, purported to be patent numbers. So we had a list of 13 seven digit numbers. That was the extent of the information provided. They demanded a sublicense agreement, and, as Attorney General Sorrell indicated, we had 2 weeks to comply. Thirty other banks in Connecticut received that same vague notice, one of which included a bank that did not even have any ATMs, so there was obviously no investigation ever conducted.

The pattern of these trolls is to send demand letters, threaten, or even file, lawsuits, and require a response within a short period of time. By forcing these settlements, they use these actions to intimidate their other targets. In fact, 2 years before we received our demand letter, this same troll brought suits in other New England states, and, because of fear and lack of resources, over 100 banks quickly settled. The following year, 80 letters were sent to Maine and Massachusetts banks. They too ultimately settled.

All of these letters were mailed, in fact, after a Federal Circuit Court upheld a lower court ruling invalidating the primary patent. Many of these banks ended up settling and paying their so-called sublicense fee, as opposed to contesting the issue, because of the cost. In some respect, in Connecticut, we were lucky. We had learned about the troll having done its work earlier in the other New England states, and we also had the advantage of hearing about some of the rulings that were coming out of the courts against this particular troll.

For my bank, the cost would have been \$27,000, which at the time represented about 10 percent of monthly earnings for the bank. For the 30 Connecticut banks targeted, had we paid together,

the amount would have been in excess of \$300,000. Even though the courts have invalidated the patents, this has not stopped this particular troll from sending demand letters, and bringing legal action against other banks in other states. I am aware that there have been additional suits filed even this year in New York and New Jersey. We thank Congress for seriously addressing this issue, and commend the House for passing H.R. 3309, the Innovation Act, which begins to address the issue, but we feel this is just the first step, and more can be done.

Chief among these is to require transparency in all allegations of a patent infringement, including details about the patent, how the target firm is infringing on it, who the real owner of the patent is, and whether the patent has expired, or been invalidated. This would help put an end to some of the abuses, while protecting legitimate patent holders. Other requirements we recommend include a registry of demand letters, and requiring bad actors to reimburse the small businesses for all fees and costs, including the costs to defend themselves.

Vendors who supply technology and equipment should be made to defend their products against patent infringement claims. Many contracts today specifically exclude such a role, and small businesses are often not in a position to force changes in that language.

In summary, the problem with patent trolls is widespread and getting worse, while the number of demand letters rises sharply each year. Fighting these trolls has a real cost, and we certainly urge Congress to take action to stop patent trolls, and protect small businesses from the enormous cost of abusive lawsuits. Thank you.

[The prepared statement of Mr. Brouillard follows:]

April 8, 2014

Testimony of

Rheo Brouillard

On behalf of the

American Bankers Association

for the hearing

"Trolling for a Solution: Ending Abusive Patent Demand Letters."

before the

Subcommittee on Commerce, Manufacturing, and Trade

of the

Committee on Energy and Commerce

United States House of Representatives



April 8, 2014

Rheo Brouillard
On behalf of the
American Bankers Association
before the
Subcommittee on Commerce, Manufacturing, and Trade
of the
Committee on Energy and Commerce
United States House of Representatives
April 8, 2014

Chairman Terry and Ranking Member Schakowsky, my name is Rheo Brouillard, Director, President and Chief Executive Officer of the Savings Institute Bank & Trust. My bank is a \$1.3 billion community bank headquartered in Willimantic, Connecticut. We serve communities throughout eastern Connecticut and Southern Rhode Island and have been in business since 1842. I appreciate the opportunity to be here to represent the American Bankers Association (ABA) regarding the impact of abusive patent demand letters on businesses. The ABA represents banks of all sizes and charters and is the voice for the nation's \$14 trillion banking industry and its two million employees.

Abusive patent litigation remains a serious threat for banks and financial institutions of all sizes across the country. Banks are often end users of technology and as a result, have been inundated by abusive and deceptive patent demand letters by patent assertion entities (PAEs), commonly referred to as "patent trolls." These patent trolls use overly broad patents, threats of litigation, and licensing fee demands in an effort to extort payments from banks across the country. These demand letters often prey on small businesses of all kinds, which do not have the resources to fight such false claims. Fighting these claims has a real cost: for banks it means less capital and fewer resources available for making the loans that drive economic growth.

At present patent trolls are able to make patent infringement claims for nothing more than the price of a postage stamp and the paper the claim is written on. These claims are often intentionally vague and based on shaky legal standing. However, when confronted with threats of expensive litigation, many banks—especially smaller banks—find that their only option is to settle, rather than paying millions to defend against extortive claims of patent infringement. Well-funded and sophisticated patent trolls take advantage of community banks with limited resources and little patent experience, and have amassed significant "licensing" fees from banks.

April 8, 2014

I have seen this first hand at my bank. We, along with 30+ other Connecticut banks, received a vague notice from a firm called Automatic Transactions LLC (ATL). The notice asserted that our ATMs operated in a way that infringed upon their “patent portfolio,” and simply listed thirteen sets of seven digit numbers as proof. What the notice failed to mention was that similar suits in other states had already been overturned. A settlement would have cost at least \$27,000 for my bank alone, and would likely have amounted to \$300,000 for the 30 Connecticut banks targeted. Fortunately, we found out about the cases that were dismissed and did not settle. My bank’s case is far from unique, and ATL is far from the only perpetrator using intimidation to target small businesses.

We thank Congress for seriously addressing this issue, and in particular commend the House for passing bipartisan legislation—H.R. 3309, the Innovation Act. This bill contains important reforms to help deal with the patent troll problem and is an important first step, but more could be done, especially by this committee. There are a number of actions that can be taken to protect small businesses against these abusive patent demand letters, which will also help protect the holders of legitimate patents. Chief among these is to ensure that more details are included, in other words more “transparency,” in any allegation of a patent infringement.

In my testimony today I would like to make the following three points:

- Patent trolls prey on small businesses, seeking to extort payments via underhanded tactics;
- The costs of “patent trolling” are real and measurable for the institutions targeted; and
- There are additional measures that Congress can take to protect American businesses while strengthening the rights of legitimate patent holders.

Patent trolls are able to prey on all small businesses¹—not just banks—because they believe that these companies lack the resources in either time or money to fight back. These targeted businesses face enormous costs from such unfounded lawsuits. We urge Congress to take action to ensure that our small businesses cannot be taken advantage of by patent trolls.

I. Patent Trolls Prey on Small Businesses, Seeking to Extort Payments Via Underhanded Tactics

Banks and small businesses of all types, face a serious threat from patent trolls that acquire portfolios of patents for the express purpose of extracting payments from anyone to whom the patent could possibly apply.

¹ ABA is working with the Main Street Patent Coalition, which consists of organizations representing banks, credit unions, retailers, app developers, hotels, restaurants, grocery stores, advertisers, direct marketers, and many other businesses that have been similarly victimized by patent trolls. www.mainstreetpatents.org

April 8, 2014

Protecting the rights of legitimate patent holders is critical for our economy; however, unlike legitimate patent holders, patent trolls use underhanded tactics to intimidate businesses into paying “licensing fees” to make them go away.

There is almost no cost for a patent troll to make a patent infringement claim. They are able to acquire numerous patents from bankrupt companies for next to nothing. They then must simply pay for the postage to send a letter alleging a patent infringement.

The letters that these patent trolls send are often purposely vague, providing little if any information that would justify the claim or enable a reasonable investigation of it. As noted above, some demand letters provide nothing more than a series of patent numbers as proof of a violation. My understanding is that in many cases there is little legal standing to their claim.

Typically, the patent troll strategy is to present a very short timeline—such as two weeks—within which to pay a settlement, threatening to escalate the action if payment is not made. The goal is clearly to scare targets into paying. Finally, to further encourage banks and other businesses to settle quickly, the patent troll will often file suit against one or more smaller entities in a particular state in order to drive settlements and serve to intimidate others in that state to settle.

Simply put, patent trolls often target small businesses believing that these companies lack the resources in either time or money to fight back. Often these companies do not have a lawyer on staff competent to evaluate the demands. Even if a business can properly evaluate a patent demand letter and determine it has no legal standing, the legal costs involved in fighting the false claim often outweigh the cost of simply paying the patent troll. Patent trolls count on small businesses to take the least costly route and pay them regardless of their legitimacy.

II. The Costs of “Patent Trolling” are Real and Measurable for the Institutions Targeted

The costs of settling allegations of patent infringement are significant for the businesses targeted by patent trolls. As I noted at the outset, my bank was targeted by just such an attack. In some respects we were luckier than other troll victims, as we learned this patent troll had already had its claims overturned in another state. But settling would have cost my bank \$27,000 plus attorney fees, which would have been a needless loss that would have had a real impact on my bank.

Let me give some specifics of this attack. On January 3, 2013, my bank, and more than 30 other banks in Connecticut, received a single page letter (Exhibit A) from a firm called Automatic Transactions LLC (ATL). This firm purported that it held a “patent portfolio” which covers the manner in which ATMs communicate over the internet. The letter included an exhibit which simply listed thirteen sets of seven digit

April 8, 2014

numbers (Exhibit B). Further it claimed that an investigation had shown that our ATMs operated in a way that made them subject to the patents. It is interesting to note that among the Connecticut banks that received this demand letter, at least one does not operate any ATMs of its own thus drawing into question the validity of the claim of having conducted an investigation.

The letter stated that the sender had sub-licensed to more than one hundred financial institutions the right to continue to operate with the patents. It added that it had thus far brought suit against approximately ten financial institutions where an amicable solution could not be reached and provided a two week window for resolution.

On January 15, 2013, I wrote back indicating that two weeks was insufficient time to conduct research into the claim and make a decision and noted that, contrary to his claim, our ATMs did not operate on the internet but were rather connected to our core IT processor by hard land based phone line. On the 17th of January ATL responded with an offer to extend his deadline until February, 4, 2013.

For the \$0.44 cost of postage and several pieces of stationary, trolls like this one prey on the fact that litigation to defend one's self against patent infringement claims are very expensive, often times reaching seven figures. This type of conduct is not an appropriate use of both the U.S. mail system the U.S. patent systems.

ATL is far from the only patent troll targeting banks, and banks are not the only industry being targeted. This is a widespread problem, with businesses of all sizes seeing such attacks. Not only is the problem widespread, but it is getting worse, with the number of demand letters rising sharply each year. The costs associated with this problem are real for American businesses of all kinds and a significant drain on the U.S. economy.

III. Congress Should Take Action to Protect American Businesses While Strengthening the Rights of Legitimate Patent Holders

The issue of abusive patent demand letters is a serious one. Thankfully, there is straightforward action Congress can take that will both protect businesses as well as legitimate patent holders. We applaud Congress for actions it has already taken on the issue, such as passing H.R. 3309, the Innovation Act. This is a good first step, but more must be done. Any action to address this issue should include the following:

First and foremost, all patent demand letters must be made more transparent. Congress should fight deceptive practices by requiring basic information be included in letters seeking to enforce patents and there needs to be an effective enforcement mechanism for this at the Federal level. Requiring greater details about the patent that is allegedly infringed, how the person receiving the letter is infringing, who the real owner of the patent is, whether the patent has expired or has been invalidated, will disrupt the business model of those that are abusing the system. Patent trolls will have to do their homework and cannot simply send out

April 8, 2014

hundreds or thousands of letters without due diligence. This would also benefit legitimate patent holders as they would know what clearly constitutes a deceptive demand letter, providing them with certainty of how to assert a patent without any risk that it could be labeled unfair or deceptive.

Second, a demand letter registry should be created and made available to the public. Any entity that sends numerous demand letters in a single year should be required to enter them into the registry. This would provide patent troll victims and enforcement authorities with the information needed to identify and take action against the trolls that are sending abusive demand letters. It would also allow those targeted in the letters to more effectively form joint defense groups by pooling their knowledge about certain patent trolls, identifying counsel familiar with these trolls, and potentially reducing defense costs.

Third, entities found to be abusing the U.S. patent system should be required to reimburse the business that they have harmed for the costs associated with fighting the false claims. As it stands now, trolls face little risk in making claims, as the worst that can happen to them is for their case to be thrown out. This would discourage them by making them liable for the costs they force upon businesses if they are found to be at fault.

Finally, vendors should take responsibility regarding allegations of patent infringement. Any legislation enacted into law seeking to remedy abusive activities by patent trolls must also deal effectively with a related dilemma facing banks and other “end users” of technology. As I have experienced, simply purchasing a product and using it in the way that was intended by the manufacturer, distributor, or producer triggered a demand letter. No business should be threatened by a lawsuit from a patent troll simply for buying a product or service that they had nothing to do with creating. Vendors should protect their customers and intervene in cases where patent trolls are making infringement allegations based on the purchase of their products or services.

Conclusion

Abusive and deceptive patent demand letters are a serious risk for businesses of all sizes across the country. Small businesses—including banks—are the most vulnerable because these patent trolls know these firms have much fewer resources or experience to defend themselves. The demand letters use deceptive and threatening language and set short timeframes for payments in an attempt to scare businesses into settlements. Congress should act and lift this unnecessary risk from the shoulders of our small businesses.

Mr. TERRY. Thank you.

Mr. Skarvan, you are now recognized for your 5 minutes.

STATEMENT OF DENNIS SKARVAN

Mr. SKARVAN. Thank you, Mr. Chairman, Ranking Member Schakowsky, and members of the subcommittee. I am testifying today on behalf of the Coalition for 21st Century Patent Reform, or 21C, a broad and diverse group of nearly 50 corporations, including 3M, Caterpillar, Eli Lilly, General Electric, Proctor and Gamble, and Johnson and Johnson. For more than 100 years, our coalition's companies have played a critical role in fostering innovation. We invest billions of dollars annually on research and development to create American jobs and improve lives. Caterpillar alone has more than 14,000 patents worldwide, either awarded, or in the approval process. Caterpillar is a company of innovation. We spend \$8 million a day on R and D.

Let me say at the outset that we believe bad faith demand letters are a problem, and we support crafting a balanced solution. Notification of patent rights are routinely presented in business to business communications to provide early notice of a patent that otherwise may not be known to the recipient. Patent demand communications can also start the clock running on patent damages. Recipients take these letters seriously in the design and development of new products and technology, oftentimes designing around the patent to avoid knowingly infringing another party's rights.

In many instances, the primary goal of the sender is simply to prevent copying, and ensure product differentiation within an industry. This is best accomplished by providing early notice, before monies are committed to substantial design and manufacturing investment, so that design-arounds are more readily accomplished. Thus, legitimate patent demand communications serve an important role in advancing technologies, providing consumers more choices, and ensuring the efficient self-policing of patent rights, preventing patent suits before they happen.

We believe that legislation on patent demand communications should address three areas of concern.

One, sanctions should be limited to those who send objectively false and misleading patent demand letter to large numbers of end-users to extort settlements. Routine business to business communications should not be swept in.

Two, clear rules of the road, with objective guidance as to what such communications should and should not contain, not a list of vague and subjective good faith and bad faith factors for a court to weigh in determining what constitutes a bad faith patent demand letter.

And finally, three, a safe harbor should be provided that clearly states what all patent owners remain free to do. By safe harbor, I mean a provision clearly informing all patent owners that they may: one, safely advise others of their ownership of, or right to license, or enforce a patent; two, to safely communicate to others that a patent is available for license or sale; three, to safely notify another, with reasonable specificity that they infringe a patent; or, four, to safely seek compensation for past or present infringement, or for a license to the patent. An appropriately crafted safe harbor

will also help to insulate any legislation from challenge on Constitutional grounds as intruding on protected free speech.

Clearly, the sending of large numbers of objectively false, misleading, and deceptive demand letters needs to be stopped. The key here is objectivity. A laundry list with a large number of subjective good faith or bad faith factors to judge whether a demand letter crossed the line must be avoided. Such lists provide no meaningful guidance to the sender of a patent demand communication. Such subjective factors will spawn unnecessary litigation, and are not likely to pass constitutional muster. Reasonable, clear, objective rules of the road are needed to guide normal business activities, rules that will not overreach and chill legitimate patent communications.

We have seen a variety of bills working their way through the states. We have seen legislation covering what I will term legitimate patent demand communications, legislation not limited to end-users, legislation without safe harbors, and legislation with vague worded factors that could sanction a perfectly legitimate patent demand communication. These differences in state legislation make it difficult, if not impossible, to provide clear guidance regarding what form of patent demand communications will be permissible nationally.

In conclusion, the public will benefit from the adoption of clear, balanced, and uniform guidance regarding the patent demand letters that constitute unfair or deceptive trade practices. This can be accomplished by the adoption of exclusive Federal legislation preempting state law directed to patent demand letters. Private enforcement under state Unfair or Deceptive Trade Practices laws should also be pre-empted, and limited to Attorney General enforcement.

Thank you, Mr. Chairman. I will be pleased to answer to any—
[The prepared statement of Mr. Skarvan follows:]



Prepared Statement of Dennis Skarvan,
Deputy General Counsel,
Caterpillar Inc.

On Behalf of the
Coalition for 21st Century Patent Reform

Before the

Subcommittee on Commerce, Manufacturing,
and Trade
Committee on Energy and Commerce
United States House of Representatives

On

"Trolling for a Solution:
Ending Abusive Patent Demand Letters"

April 8, 2014

SUMMARY

The Coalition for 21st Century Patent Reform (21C) agrees that “bad-faith demand” letters are a problem and supports solutions to address them, but legislation in this area must reflect caution and balance. Appropriately “targeted” legislation will curtail the egregious practices that have developed whereby some patent owners send thousands of letters to small businesses with false or misleading threats of litigation for patent infringement and demand payment. Unfortunately, some legislative proposals to correct these abuses sweep in business-to-business communications and inadvertently chill legitimate patent communications. Efforts to address what is a relatively small number of egregious patent demand letter abuses should preserve legitimate patent communications in which patent owners normally engage.

The U.S. patent system is designed to encourage notice and communication of patent rights and to foster respect for patent rights. It is an efficient way to guide innovation around others’ patent rights to avoid or resolve infringement disputes without the need to file lawsuits, as well as to expand licensing and technology dissemination. Patent owners engaged in legitimate patent licensing communications have no desire to deceive or mislead any recipients.

Many of the proposals addressing written communications contain no meaningful limits to protect patent owners legitimately communicating their rights. The enforcement authority of the FTC and state Attorney Generals should not be invoked against patent owners in such cases. It should be reserved for those situations where hundreds of bad faith letters are sent to “end-users” who purchase merchandise in the ordinary course of their trade or business and who do not resell it. Such limits would further their consumer protection roles and reduce the risk that they would be drawn into individual patent disputes.

Some proposals would require patent owners to include burdensome and unnecessary details in any patent letter, far more than necessary to inform an infringer of the patent owners’ concerns. They include factors that a court could consider as evidence in bad faith that are wholly subjective, and would apply to all communications, not just those to small business end users. Such proposals will spawn unnecessary litigation, and are unlikely to pass Constitutional muster. Reasonable and clear rules of the road are needed to guide normal business activities; rules that will not inadvertently deter legitimate patent communications.

Any legislation crafted to protect small business end users from “patent trolls” should include a “safe harbor” to ensure that customary business communications of innovative companies are not impacted. An appropriately crafted safe harbor will also help to insulate any legislation from challenge on Constitutional grounds as intruding on protected free speech rights.

The interests of balance, uniformity and clarity apply nationally and would be furthered by the adoption of exclusive federal legislation preempting state law or regulation directed to patent demand letters. Federal preemption should also prevent the prospect of private enforcement under state unfair or deceptive trade practices laws.

Mr. Chairman and distinguished Members of the Subcommittee:

Thank you for the opportunity to appear today as a representative of the Coalition for 21st Century Patent Reform ("21C") and to testify on the subject of abusive patent litigation practices, and their impacts on American innovation and jobs.

Introduction

By way of introduction, I am the Deputy General Counsel in Caterpillar's Legal Services Division responsible for Caterpillar's Worldwide Intellectual Property practice. Caterpillar has roughly 14,000 patents worldwide - either awarded or in the approval process. We are a company of innovation - we spend \$8 million a day on R&D.

I am testifying today for the 21C, a broad and diverse group of nearly 50 corporations including 3M, Caterpillar, Eli Lilly, General Electric, Procter & Gamble and Johnson & Johnson. For more than 100 years, our Coalition's companies have played a critical role in fostering innovation. We invest billions of dollars annually on research and development to create American jobs and improve lives. Representing 18 different industry sectors, including manufacturing, information technology, consumer products, energy, financial services, medical device, pharmaceutical, and biotechnology, our Coalition advocates for patent reforms that will foster investment in innovation and job creation and promote vigorous competition in bringing new products and services to American consumers.

Opportunistic sending of demand letters by "patent trolls" is a problem

Let me state at the outset that the 21C acknowledges that "bad-faith demand" letters are a problem and we support solutions to address them. We too experience these so-called "patent trolling practices." At the same time, however, we also need the ability to protect our hard-earned patents. We need the right - without violating the law - to send letters to those who are infringing our patents. There is a distinct and critically important difference between patent assertion entities or "patent trolls" who mass mail letters to small businesses, retailers and banks - hoping to "score" settlements based solely on intimidation - and hundreds of valid patent holders, including individual inventors and universities, placing the public on notice of their patent portfolios, offering their patents for license, and, when necessary, protecting their patented products from being infringed.

According to our information, legislation addressing bad-faith demand letters has either been enacted or sent to the governor for signature in eight states and is under consideration in eighteen other states. We have been and will continue working diligently in the states, where we and other 21C member companies have a presence, to find a "workable" and practical solution to the problem. We will continue to work with the states and with Congress to develop a single set of rules, to ensure a high degree of uniformity and consistency nationally, that parties can confidently follow without being subject to a myriad of varying, and likely inconsistent, laws and rules promulgated by different states.

Remedies should reflect caution and balance

Appropriately "targeted" legislation will curtail some of the egregious practices that

unfortunately have developed whereby some patent owners send upward of hundreds - or even thousands - of letters to small businesses or individuals with false or misleading threats of litigation for alleged patent infringement and demand payment. Unfortunately, not only has federal legislation been proposed, but state laws have also been proposed, and in some cases enacted, that will sweep in business-to-business communications and inadvertently chill legitimate patent communications. Legislation in this area should reflect caution and balance. Efforts to address what is a relatively small number of egregious patent demand letter abuses should preserve legitimate patent communications that Caterpillar and other patent owners engage in as part of their normal business communications.

The U.S. patent system is designed to encourage notice and communication of patent rights and to foster respect for patent rights. It does this as an efficient way to guide innovation around others' patent rights to avoid or resolve infringement disputes without the need to file lawsuits, as well as to expand licensing and technology dissemination. Patent owners engaged in legitimate patent licensing communications have no desire to deceive or mislead any recipients of their communications. To the contrary, it is in their interest to provide early and sufficient information to make clear their ownership of the patent rights in question and their intentions to either license or enforce those rights. That is why the vast majority of patent owners send patent "enforcement" letters. These communications are self-policing by providing notice of another's patent rights of which the recipient of the letter may simply not be aware. Manufacturers appreciate receiving early notice of others patent rights in areas in which they may be planning to invest so that they can make changes or take a license to avoid a later infringement action.

Many of the legislative proposals address written communication which states that the intended recipient or any person affiliated with the intended recipient is, or may be, infringing a patent. These measures contain no meaningful limits to protect patent owners legitimately communicating their rights. They cover ANY written communication regarding patent infringement, made to anyone. The enforcement authority of the Federal Trade Commission (FTC) should not be invoked against patent owners legitimately communicating their rights. It should only be invoked in those situations where hundreds or even thousands of bad faith letters are sent to small businesses, retailers, banks, or individuals who are "end-users" who purchase merchandise, or contract for the purchase of merchandise, not for resale in the ordinary course of their trade or business. Limiting the FTC's enforcement authority to these abusive situations furthers its consumer protection role while reducing the risk that the FTC will be drawn into individual disputes between patent owners and potential licensees or alleged infringers. Such "one-off" disputes should be decided by Federal Courts applying substantive patent law, not by the FTC under their consumer protection authority.

Customary business communications should be protected by a "safe harbor"

In order to mitigate the risk of adversely affecting deterring legitimate patent licensing and enforcement communications, any Federal, or for that matter any state, legislation crafted to protect small business and individual end users from the abusive practices of so-called "patent trolls" should include a "safe harbor" provision to ensure that customary business communications of innovative companies are not impacted. Such a provision should make it clear that the legislation is not intended to

impinge on a patent owner's right to put others on notice of its patent rights and the availability of, or need for, a license.¹ An appropriately drawn safe harbor provision will also help to ensure that the legislation is not vulnerable to challenge on Constitutional grounds as too intrusive upon protected rights of free speech in connection with legitimate patent licensing and enforcement activities.² Otherwise, there is a real risk that well-intended provisions, or the entire act itself, will be struck down on the grounds that the Constitutional rights of free speech and to petition our government has been abrogated by provisions seeking to mandate to patent owners what they must say when communicating information, rather than limiting those provisions to restrict them from making false and/or deceptive statements.

Prospective solutions should not unnecessarily burden patent owners

Some pending legislative proposals would impose a burdensome and unnecessary list of requirements that must be included in any patent letter, far more than what would be necessary in the normal course for a patent owner to adequately inform an infringer of the patent owner's concerns. It would hamper or even stop a patent owner's ability to send legitimate demand letters. For example, language in one proposed bill calls for "a clear, accurate, and detailed description, such as the manufacturer and model number, of each product, device, business method, service, or technology that allegedly infringes each claim." Patent claims are often lengthy

¹ See, e.g., *Virtue v. Creamery Package Mfg. Co.*, 227 U.S. 8, 37-38 (1913) ("Patents would be of little value if infringers of them could not be notified of the consequences of infringement, or proceeded against in the courts. Such action, considered by itself, cannot be said to be illegal."); *Va. Panel Corp. v. MAC Panel Co.*, 133 F.3d 860, 869 (Fed. Cir. 1997) ("[A] patentee must be allowed to make its rights known to a potential infringer so that the latter can determine whether to cease its allegedly infringing activities, negotiate a license if one is offered, or decide to run the risk of liability and/or the imposition of an injunction.").

² Courts have held that patent demand letters fall within the First Amendment's guarantee of "the right of the people . . . to petition the Government for a redress of grievances," U.S. Const. amend. I, and thus are protected from liability by the Noerr-Pennington doctrine. See, e.g., *In re Innovatio IP Ventures, LLC Patent Litig.*, 921 F. Supp.2d 903 (N.D. Ill. 2013) (collecting cases).

and very detailed, and in many cases companies simply do not have access to a competitor's product or technology to provide such information. For example, Caterpillar's surface and underground mining patent portfolio could cover a competitor's machine located in a remote mine site, or Caterpillar's advanced manufacturing technology patent portfolio could cover activities inside a competitor's manufacturing facility to which we have no access. Such detail is not available without discovery in litigation.

Solutions should be focused on surgically fixing the problem

The definition in some of these legislative proposals, regarding communications of possible patent infringement that a court "may consider" as evidence that an assertion was made in bad faith, are filled with wholly "subjective factors." Moreover, the definitions make communications to anyone, not just to small business end users of products who have no intention of reselling them, subject to sanctions. Some of these proposals would have the determination of whether a demand letter constitutes an unfair or deceptive act dependent on factors such as whether the response time is "unreasonably short," whether the amount proposed for a license is a "reasonable estimate," whether the claim of infringement was "meritless" or whether it is "likely to materially mislead a reasonable intended recipient." Such vague and indefinite restrictions on patent owner's right to inform others of their patent rights will spawn unnecessary litigation, and are unlikely to pass Constitutional muster.

Patent communications are like other business activities in the sense that what is needed are reasonable and clear rules of the road to guide normal business

activities. The definition of assertions that would constitute an unfair or deceptive act which are so nebulous, as they are in many of these proposals, that they leave patent owners pursuing legitimate enforcement and licensing activities without clear guidance as to what they can and cannot communicate to infringers and potential licensees are equally troublesome. The appropriate goal of legislation in this area should be to identify, and empower the FTC to address through its enforcement powers, only those demand letters which are truly intended to deceive or mislead their recipients. For example, a demand letter may be considered to be objectively false or misleading if it falsely states that litigation has been filed against the recipient or there is a widespread pattern of such threats being made where the sender knows that no litigation has been filed. Similarly, a demand letter that seeks compensation for a patent that has not been issued, or that has been held to be invalid, or has expired could be considered to be objectively false or misleading.³

Legislation in this area should reflect caution and balance to ensure that efforts to address what is a relatively small number of egregious patent demand letter abuses do not inadvertently chill legitimate patent communications that patent owners engage in each and every day.

Federal preemption is needed to ensure certainty and uniformity

The public, and patent owners alike, will benefit from the adoption of clear, balanced and uniform legislative guidance regarding the FTC's authority to target bad-faith patent demand letters that clearly constitute unfair or deceptive trade practices within

³ For a more complete list of objectively false and materially misleading assertions found in deceptive demand letters, see Statement of Philip S. Johnson, "Protecting Small Businesses and Promoting Innovation by Limiting Patent Troll Abuse," Judiciary Committee of the United States Senate, December 17, 2013, available at <http://www.patentsmatter.com/issue/pdfs/JohnsonSenateJudiciaryCommitteeStatement20131217.pdf>.

the meaning of Section 5(a)(1) of the Federal Trade Commission Act. These interests of balance, uniformity and clarity apply nationally and are furthered by the adoption of exclusive federal legislation. Just as substantive patent laws derive from the Constitution and are exclusively within the province of Federal statutes and courts, so too should issues relating to consumer protection against patent demand letters be applied consistently and uniformly nationwide through federal legislation, regulation and judicial action. Thus the FTC, rather than individual states, appears to be in the best position to weigh the balance that federal legislation establishes between the need for consumer protection against bad faith demand letters and the need to ensure that we do not weaken our patent system by making patent licensing or enforcement more difficult or less certain. Legislation in this area should expressly provide that it preempts state law or regulation directed to patent demand letters.

Federal preemption should also prevent the prospect of private enforcement under state unfair or deceptive trade practices laws. Private enforcement does not further consumer protection and it heightens the risk that one of the more "sophisticated" infringers to whom we send a letter will file suit to exert leverage in our private patent dispute. In such cases, not only might the infringer be able to continue with its infringement, it may even get a "windfall" in the form of exemplary damages. This should be avoided so as to not tilt the playing field in favor of infringers, and against inventors and patent owners, in a way that goes well beyond what's needed to protect against so-called "patent trolls."

Conclusion

The 21C is prepared to work with the Committee on Energy and Commerce, other

House Committees, as well as with Members of the Senate to assist in the drafting of legislation, consistent with foregoing principles, to provide guidance for the FTC, using its existing authority, to sanction such abusive bad faith demand letter practices while ensuring that legitimate patent communications are not inadvertently discouraged.

Mr. TERRY. Thank you, Mr. Skarvan.
Mr. Schultz, you are now recognized for your 5 minutes.

STATEMENT OF JASON SCHULTZ

Mr. SCHULTZ. Thank you, Chairman Terry, and Ranking Member Schakowsky, and members of the subcommittee. And, again, apologies for my delay getting here.

At NYU Law I run a law and technology policy clinic, and for some people that is a bit of a confusion. They are like, what do you mean? What is a pro bono clinic doing in the law and technology area? Well, one of the things we do is we get a lot of e-mails and phone calls from some of these people who have received demand letters and can't afford to hire a patent attorney, and they want to know what to do.

And I can tell you from my experience, now over 10 years generally, but specifically 7 years running pro bono clinics such as these, that, when I look at the letter, if it is some vague letter that doesn't actually specify what the accusations of infringement are, sometimes what all the patents are, and the claims at issue, it is hard for me to tell. It is hard for me to tell them anything. It is hard for my students, who I am supervising, and trying to teach to be lawyers, to tell them anything. And that is why I think this issue is very important, and I am very glad the subcommittee is taking it up, because this is not just about the shakedown. This is not just about the end-user or the small business who receives a letter, but it is also about helping them, if they can find help, to have the attorneys be able to advise them.

It is one thing to defend a patent litigation, and we have seen a lot of statistics about how many millions of dollars that takes, but sometimes you can resolve these issues in good faith, if you have enough information. So I just want to highlight that this is about an intermediate step, as much as a final step, in sort of looking at this problem broadly.

Now, who are the people who receive demand letters? You have heard about a number of folks who are in very precarious situations when they receive these letters. My clinic and my students, we often will advise very small entrepreneurs in terms of the size of their operation. These will be application developers who are just writing something for the iTunes or Google App store. They will be mom and pop Web sites who are trying to develop their own content. Some of these patents actually cover content, and the use of content, and how it interacts with technology. And some of them will be community projects. We have seen a lot of work right now developing civic technology to try and improve roads, to try and improve use of data, and look at the environment, improve water quality. They are all receiving patent demand letters too, many of them just as vague as the ones you have been hearing about.

So in this role, there are sort of two problems that I think this committee could address. One is, as we have heard, that there are these vaguenesses that in some ways can even be deceptive when they are being asserted as a guaranteed infringement. So the patent owner will send a letter, say, you infringed this patent, but won't explain why, when I don't think even the patent owner knows, because this will be part of a campaign of general assertion,

not specific to any individual or entity, but just, we believe this whole group of people out there somehow infringed. And they assert it as if it is the truth, but they don't even know, and that, to me, is deceptive. And the second is, as we have heard, when they have no intention to sue whatsoever, that the threats made are intimidating, and put the recipients in a position where they don't actually know what their options are.

So when looking at this, I think we have just started to collect information about the problem, and I just want to say that efforts to try and collect more demand letters, such as trollingeffects.org, have been somewhat successful, but I would like to see more information so we can understand the scope of the problem.

But turning to the solution, I think that, for me, these letters should be required to have specific allegations and information in them so that the recipient can look at them and assess what is actually going on, what are they being accused of? Several of the small entrepreneurs, and coders, and developers that I have talked to, they are actually technical people. They could actually try and figure this out, but they look at the letter, and they say, I have no idea what they are talking about.

And part of that is not just because the patent is vague, but because there is no information about what that patent owner thinks that this small coder did, or what the application that they put up on the iTunes store does that they think infringes. And so that information would be extremely helpful, and to require that, to require the patent owner to do their homework, to look at what this recipient has done, would be extremely helpful for the people that my students and I help.

I think it would also help those who are recipients of good faith demand letters as well, because let us say you do actually infringe the patent. Well, you should then figure out, are you going to design around it? Are you going to pay the license? Are you going to fight the patent because you believe it is invalid, even though you might actually fall into the claims? Those are legitimate decisions, and, again, more information early on helps resolve this at the lower cost.

The other thing is that our public patent system is a public notice system. And I just want to reinforce that, as my final point, to say that it is as much about what the patent says when it is published at the Federal Register, but also when a patent owner is asserting it, they are asserting a public grant to them of a property right. And I think that the meets and bounds of that assertion, and when you trespass on it, should be as clear as anything else. Thank you.

[The prepared statement of Mr. Schultz follows:]



New York University

A private university in the public service

School of Law
Faculty of Law

245 Sullivan Street, Room 609
New York, New York 10012-1301
Telephone: (212) 992-7365
E-mail: jason.schultz@nyu.edu

Jason Schultz

*Associate Professor of Clinical Law
Director, Technology Law & Policy Clinic*

**Committee on Energy & Commerce
Subcommittee on Commerce, Manufacturing, and Trade
U.S. House of Representatives**

Hearing:

“Trolling for a Solution: Ending Abusive Patent Demand Letters.”

**Testimony of Jason Schultz
Associate Professor of Clinical Law
NYU School of Law**

April 8, 2014

Testimony of Jason Schultz
Associate Professor of Clinical Law, NYU School of Law

Before the
House Energy & Commerce Committee
Subcommittee on Commerce, Manufacturing, and Trade

Hearing:
“Trolling for a Solution: Ending Abusive Patent Demand Letters.”

April 8, 2014

Chairman Terry, Ranking Member Schakowsky, and Members of the Committee, thank you for holding this hearing and inviting me to testify today about ending abusive patent demand letters.

I am an Associate Professor of Clinical Law at New York University School of Law, where I teach a Technology Law & Policy Clinic. In my clinic, law students represent individuals, non-profits, and startups on a range of legal issues, including defending themselves against abusive patent threats. My clinic is also a member of the Application Developer Alliance’s Law School Patent Troll Defense Network, a nationwide group of law schools, law students, and lawyers, working together to provide free legal services to individual and startup software developers and other small business entrepreneurs who are threatened by patent trolls.¹ Prior to teaching, I served as a Senior Staff Attorney at the Electronic Frontier Foundation, where I founded the Patent Busting Project, an effort to help individuals and small businesses fight back against abusive patent threats, and before that, I worked as a patent litigation associate at Fish & Richardson, one of this nation’s oldest and most respected intellectual property firms. In total, I have over 10 years of experience defending clients against patent threats, including dozens of demand letters.

Patent trolls (also known as Patent Assertion Entities, or PAEs) are causing enormous harm to innovators and consumers for many reasons. They are often attacked by trolls who purchase vague and overbroad patents to launch or threaten lawsuits. One particular type of troll, which some have labeled “bottom feeders”² harms businesses and consumers in a particularly nefarious way – through dangerous and irresponsible demand letter-writing campaigns. Indeed, as the White House found: “The PAE business model is based on the

¹ See <http://devsbuild.it/trolldefensenetwork>.

² Mark A. Lemley & Douglas Melamed, *Missing the Forest for the Trolls*, 113 COLUM. L. REV. 2117, 2126 (2013).

presumption that in many cases, targeted firms will settle out of court rather than take the risky, time-consuming course of allowing a court to decide if infringement has occurred.”³

These demand letters are often vague, lacking basic details such as which claims of the patent are at issue. They also rarely explain or describe in detail exactly how the recipient’s product or service infringes. Faced with such threats, many entrepreneurs have no way to evaluate the legitimacy of the claim, let alone the appropriate value of any settlement offer. And even though a demand letter is not a legal complaint, and even if it makes specious claims, the mere threat of litigation brings with it serious costs. As one study found:

Patent demands can be costly to resolve, and particularly so for small companies. The overwhelming majority of companies said that resolving the demand required founder time (73%) and distracted from the core business (89%); most experienced a financial impact as well (63%). However, responses and the costs of these responses ran the gamut; for example, 22% of those surveyed said they “did nothing” to resolve the demand.⁴

So, rationally, many simply settle and pay licensing fees that may not even apply to the technology they are building or using.

How to Help:

Require Patent Owners to Do Their Homework Before Sending a Demand Letter

The primary way this Committee can act to help fix this problem is to require patent owners to do their “homework” before sending a demand letter.

Companies that actual invent patentable products and services are no strangers to competition. They understand that they need to innovate *and* study the competition in order to stay ahead of the curve. Most if not all entrepreneurs, especially in the tech sector, follow competing products and services very closely, both from an engineering and marketing perspective. Thus, if they find a product or service that infringes one of their patents, it is not very costly to describe how that product or service infringes in letter form. They’ve already done their homework for business reasons.

³ Executive Office of the President, *Patent Assertion and U.S. Innovation*, at 12, http://www.whitehouse.gov/sites/default/files/docs/patent_report.pdf

⁴ Colleen V. Chien, *Startups and Patent Trolls* (Santa Clara Univ. Sch. of Law Legal Studies Research Paper Series, Accepted Paper No. 90-12, 2012) at 10, (“Chien 2012”), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2146251.

Bottom-feeding trolls, on the other hand, rarely do their homework. They do not compete with companies in the marketplace; all they care about is threatening them and their users with court actions. They simply fire off boiler-plate demand letters to any conceivable recipient, hoping to maximize their return by preying on as many victims as possible, with as little effort as possible. It's a shotgun approach; there are no extra points or profits for accuracy.

To impose a "homework" requirement of actually analyzing the accused product or service disrupts this equation and makes many forms of "bottom feeder" trolling less profitable and thus less appealing. By raising the marginal cost per demand letter, the model breaks down. On the other hand, legitimate patentees who are already engaged in market research and competitive analysis have nothing to fear from this requirement.

So what would constitute such due diligence? At their core, reasonable demand letters would provide four pieces of information: (1) the specific patent numbers and claims asserted; (2) the specific products or services accused of infringing; (3) a "claim chart" explaining how the accused product or service satisfies every element of every asserted claim; and (4) patent status information, including whether the patent is currently part of any administrative or judicial proceeding and who has a financial stake in exploitation of the patents described.

For enforcement of non-compliance, there are many options. In my mind, the easiest would be unenforceability of the patents or claims listed, a remedy already available for forms of "patent misuse." One could also craft it as a standing requirement for bringing suit, much like copyright registrations are required in copyright infringement lawsuits under 17 U.S.C. § 411. One could also impose fines or encourage enforcement actions by federal or state agencies that police unfair and deceptive trade practices.

In closing, I wish to thank you again for inviting me to participate in this hearing and would be pleased to answer any further questions you might have for me.

Mr. TERRY. Thank you.

Mr. Chandler, you are recognized for 5 minutes.

STATEMENT OF MARK CHANDLER

Mr. CHANDLER. Thank you, Chairman Terry, Ranking Member Schakowsky, members of the subcommittee. My name is Mark Chandler. I am General Counsel of Cisco Systems. I am here today to describe our experience with a new kind of scam. I am talking about a rip-off that is based on a formula that is as old as the hills, but dressed up as patent infringement and innovation protection. The scam artists, as you have heard, send out thousands of letters not to me, but to my small business customers, and they file lawsuits in the hope of a payday not based on the merits of the case, but on the fears of victims who just want a problem to go away. These victims, mom and pop stores, community banks, hospitals, car dealers, restaurants, aren't manufacturers of products. I do that. They are simply users, like you and me in our private lives.

As Cisco's chief legal officer, I want to defend my customers, but we need your help in bringing some light, some sunshine, to these nefarious practices. Cisco was founded 30 years ago to build products so incompatible computer systems could talk to each other. Today we are the world's largest manufacturer of Internet equipment, from backbone switches, to phone and video systems. Our annual revenue is about \$50 billion, and we directly or indirectly provide jobs to hundreds of thousands of Americans. Our products are used literally by billions of people around the globe, and are in tens of millions of American homes and businesses. We spend more than \$7 billion a year on research and development. We hold over 10,000 individual U.S. patents. We believe in a strong patent system.

Now let me tell you a story which, unfortunately, is not unique. The story is not about patents. It is about using patents as the cover for a scam. Our story begins when a lawyer named Noah Whitley bought patents related to Wi-Fi from a great American chip maker, Broadcom, and created an entity that I think the somewhat cynically named Innovatio. Broadcom, for its part, didn't want the patents anymore, since they were near expiration, had been broadly cross-licensed to other chip companies, and were subject to binding contracts requiring licensing on fair terms.

But Whitley wasn't deterred by that. He and his lawyers sent 14,000 letters to small businesses, cafes, bakeries, inns and hotels, a children's health clinic, basically anyone that might use Wi-Fi in their place of business. Did he tell them what specific products they had might infringe, might have? Not even a list of types of products? No. Instead, his lawyers just wrote, "I represent an individual who has suffered injuries as a result of your company's business," and claiming that the Innovatio portfolio covers all Wi-Fi usage.

Did his lawyers disclose that a huge proportion of Wi-Fi devices were already licensed, and therefore no more could legally be collected on those patents? No. Instead, he told them that almost a billion dollars had been collected in royalties on those patents, that thousands of companies had paid, without letting on that almost all

those royalties were exclusively collected by Broadcom in cross-licenses that had little or nothing to do with these patents.

Did they tell them that the patents related to industry standards, and had to be licensed on fair terms? No. Instead, they told them, and again I quote, “We wish to license your company at a very affordable rate, far less than the cost of patent litigation. I can quote you a rate of less than \$3,000 per location.” This for patents that a court later determined were worth pennies per chip, and equipment that these businesses had spent, at most, a few hundred dollars to buy.

And did they tell them that manufacturers, like my company, were eager to defend them? No. Instead, they wrote that equipment manufacturers have not stepped in to defend any of their users. This means we can still sue your client, and they cannot expect equipment manufacturers to aid in their defense.

Finally, for those who had the temerity to resist, they enumerated thousands of pages of documents that they said needed to be reviewed, meaning a mountain of legal fees. Now, sadly, this isn’t an isolated incident, as General Sorrell, Mr. Brouillard, and others in the panel can tell you, but a dangerous trend.

Let me close by suggesting four simple steps that would make it much harder to carry out these schemes. First, requiring anyone sending more than 10, or some other number of patent demand letters to someone who is not a manufacturer or re-seller of the product to file the letters in an online registry, so they are easy to find. Second, require them to include a list of model numbers which they believe infringe, the fact that the manufacturers may be required to defend, and contact information for the manufacturers. Third, require any such letter to include the names of the real entities or individuals who own the patents. And fourth, require the letters to include a list of all previous licenses, and whether the patents are subject to special licensing rules that apply to industry standards.

While the FTC can already investigate and sue the most egregious patent scam artists, these simple steps will provide a basic level of transparency to protect innocent end-users. Requiring full disclosure about what is being offered for sale doesn’t violate anyone’s free speech. I stepped into that case, and I spent \$13 million of my company’s money to put a stop to this. The paycheck I get every other week says Cisco on the top of it, but every cent of it comes from my customers. That is why I am here today. That is why I am passionate about making sure they don’t get ripped off by charlatans dressed up as innovators when they trust us to supply them with products.

And, Mr. Chairman, if the predators are forced to come to me, once they have disclosed what they are after, I can guarantee they will get a fair fight. Thank you.

[The prepared statement of Mr. Chandler follows:]

Prepared Statement of Mark Chandler
“Trolling for a Solution: Ending Abusive Patent Demand Letters”
April 8, 2014

Chairman Terry, Ranking Member Schakowsky, members of the Subcommittee, I am grateful for the opportunity to appear before you today and describe our experience with a new kind of consumer scam that we are seeing with increasing frequency.

Deceptive behavior of this kind has long existed but now comes clothed in language like “patent infringement” and “innovation.” The goal is the same as in many old-fashioned consumer rip-off schemes that the government has long taken action against – trying to scare or convince people to pay something they don’t owe or buy something they don’t need. The direct victims are not large companies like Cisco Systems, but small businesses, non-profit organizations and individuals.

I am involved because I need to defend my customers. But we need your help.

We need a little sunshine to disinfect this dark corner of the patent world because once the practices used by these scam artists are exposed, and the harm to their victims better understood, these rip-off artists will be forced

to change their ways.

Introduction

I am Senior Vice President and General Counsel of Cisco Systems. We are a 30-year old company, founded by two Stanford graduate students, who developed the key technology to allow different computer systems to communicate with each other.

Our products are used every day by billions of people around the world, and we sell everything from the core switches and routers that make up the backbone of the Internet, to Wi-Fi systems people use in their homes and businesses, to telephone and video conference systems used by tens of millions of businesses and consumers.

Our annual revenue is approximately \$50 billion, and we directly employ approximately 37,000 people in the United States and indirectly provide jobs to hundreds of thousands more.

We hold over 10,000 U.S. patents and file many hundreds of new patent applications every year. Our patents portfolio is regularly rated among the strongest in the telecommunications industry. Most importantly, our products are used in tens of millions, and perhaps over 100 million, American homes and businesses.

Unfortunately, I have appeared all too many times before Congress on this topic, having testified last year in front of your colleagues on the Senate Commerce Committee¹ as well as the Judiciary Committee about the scourge of abusive patent litigation practices.²

I am pleased to report that since then, the House, with the support of many of the members of your Committee, passed a strong, comprehensive patent reform bill with the Innovation Act by an overwhelmingly bipartisan vote. Additionally, as I sit before you today, your colleagues in the Senate Judiciary Committee are working through legislation that will hopefully mirror many of the House's provisions and make patent litigation fairer and more efficient.

We are also hopeful that your colleagues on the House Ways and Means Committee and their counterparts on the Senate Finance Committee will soon work to assure that International Trade Commission procedures can no

¹ *Demand Letters and Consumer Protection: Examining Deceptive Practices by Patent Assertion Entities; Hearing before the Senate Commerce Committee (Nov. 7, 2013)* (statement of Mark Chandler), available at http://www.commerce.senate.gov/public/?a=Files.Serve&File_id=1f96ee66-3e13-421a-aac5-2dc7a0a87da1 (last visited Apr. 3, 2014).

² *Abusive Patent Litigation: The Impact on American Innovation & Jobs, and Potential Solutions; Hearing before the House Judiciary Committee (Mar. 14, 2013)* (statement of Mark Chandler), available at [http://judiciary.house.gov/_files/hearings/113th/03142013_2/Chandler 03142013.pdf](http://judiciary.house.gov/_files/hearings/113th/03142013_2/Chandler%2003142013.pdf) (last visited April 3, 2014).

longer be used for shakedowns by non-practicing entities that do not truly want an exclusion order. Exclusion orders are the only remedy available from the I.T.C., but often non-practicing entities only want to leverage the threat of such an order to obtain money to which they are not entitled.

These reforms, which focus on litigation abuses, however, don't address the kind of rip-off I'm describing today – a rip-off that targets small businesses and consumers with threat letters, deception, and intimidation tactics.

Examples: Innovatio

Our first story begins with a lawyer named Noel Whitley, who bought patents related to Wi-Fi from his former employer – a great American chip company, Broadcom – and then worked with a team of Chicago lawyers, the Niro firm, which specializes in representing patent assertion entities, to target legitimate businesses.

He created a company which he cynically called “Innovatio,” since innovation is the last thing that the company does. Broadcom sold the patents because they were near their expiration date, heavily licensed to Broadcom's competitors and subject to binding commitments to license on fair and reasonable terms.

So Mr. Whitley and the Niro firm came up with a scheme. He sent over

14,000 letters to small businesses, cafes, bakeries, inns and hotels, a children's health clinic – anyone who he thought might be using Wi-Fi.

Mr. Whitley's team of lawyers and licensing "consultants" told these non-profits and small businesses: "I represent an individual who has suffered injuries as a result of your company's business." They went on to say, "We are highly confident that the Innovatio portfolio covers effectively ALL currently implemented embodiments of Wi-Fi technology in use today."

They didn't tell them that a huge proportion of Wi-Fi devices were already licensed, because of Broadcom's cross licenses and the license Broadcom kept for itself, and that therefore they might not even need any further permission or licenses from Innovatio. Instead, they claimed that almost a billion dollars had been collected in royalties already; referring mostly to amounts paid to Broadcom by its arch-competitor Qualcomm to resolve numerous U.S. and foreign legal claims that had almost nothing to do with these patents.

They also claimed that thousands of companies had already paid Innovatio as well. They didn't tell their targets that the patents related to industry standards and therefore had to be licensed on fair and non-discriminatory terms – something that all three of the former owners including Broadcom

had irrevocably promised to do. Instead they told them, that “[W]e wish to license your company at a very affordable rate – far less than the cost of patent litigation. I can quote you a rate of less than \$3000 per location” – this for patents that a Federal court recently determined were worth pennies per chip.³

And he didn’t tell them that the manufacturers of the products, including Cisco, were suing Innovatio to defend their customers. Instead he misrepresented to them that the equipment manufacturers, “have not stepped in to defend any of their users. This means we can still sue your client and they cannot expect equipment manufacturers to aid in their defense.”

Finally, for those businesses who had the temerity to resist, Innovatio enumerated thousands of pages of documents that would have to be reviewed by counsel to even begin to defend against Innovatio’s allegations, meaning thousands of dollars in legal fees. Unfortunately, thousands of businesses may have fallen for this scam.

So, although Innovatio cloaks its business in the patina of patents and patent

³ *In re Innovatio IP Ventures, LLC Patent Litig.*, MDL No. 2303, 2013 WL 5593609 (N.D. Ill. Oct. 3, 2013).

infringement, the reality is that Innovatio is just a modern take on an old scam.

Innovatio conducts its racket by sending letters containing mistruths and omissions to thousands of consumers in an attempt to obtain money from these targets to which Innovatio is not entitled.

And, unfortunately, Innovatio is only one example of this emerging type of consumer fraud.

Project Paperless/MPHJ

There have been numerous news articles about a similar scam by an entity that originally was called Project Paperless and which ultimately became known as MPHJ. Project Paperless engaged in a letter-writing campaign demanding \$1,000 per employee from their targets.⁴ An online project⁵ discovered that some of the partners in Project Paperless's law firm likely had an ownership interest in the patents. Soon after the revelation of this inconvenient truth, Project Paperless dropped its lawsuits and sold the

⁴ See Joe Mullin, *Meet the nice-guy lawyers who want \$1,000 per worker for using scanners*, arstechnica (Apr. 7, 2013), available at <http://arstechnica.com/tech-policy/2013/04/meet-the-nice-guy-lawyers-who-want-1000-per-worker-for-using-scanners/> (last visited April 3, 2014).

⁵ See Stop Project Paperless website - <http://project-paperless.com/the-patents/> (last visited April 3, 2014).

patents to another shell company called MPHJ Holdings, after which threatening letters started coming from a full alphabet soup of strangely named shell companies including AccNum, AllLed, AdzPro, CalNeb, ChaPac, FanPar, FasLan, FulNer, GosNel, and HunLos.

State attorneys general in Minnesota, Nebraska, New York and Vermont as well as the FTC have taken various actions against MPHJ to protect business and consumers in their respective states from MPHJ's deceptive practices. For example the Vermont attorney general's action against MPHJ lists MPHJ's lies and abusive practices in gory detail including:⁶

1. MPHJ entities sent threatening letters without doing any actual investigation of whether their patents were being infringed.
2. MPHJ forced its targets to do the work of analyzing infringement
3. MPHJ deliberately targeted small businesses without ready access to sophisticated representation
4. MPHJ told its targets that it had a successful established licensing program when in fact it had signed very few licenses with an average licensing fee of \$900.
5. MPHJ's letters indicate that litigation would be imminent if a license deal was not signed almost immediately yet MPHJ had never actually

⁶ Consumer Protection Complaint in *Vermont v. MPHJ Technology Investments, LLC*, No. 282-S-13WNCV (Vt. Super. Ct.) (filed May 8, 2013), available at <http://www.atg.state.vt.us/assets/files/Vermont%20v%20MPHJ%20Technologies%20Complaint.pdf> (last visited April 3, 2014).

filed suit.

Minnesota reached a settlement with MPHJ forcing them to cease and desist from targeting Minnesota businesses.

Helferich

Cisco also is aware of another such entity, Helferich Patent Licensing, LLC (“Helferich”). Helferich was founded in 2007 “for the purpose of commercializing, licensing, and enforcing” patents relating to delivery of content to a cell phone. Although Helferich had already licensed its patents to cell phone manufacturers, it sought to double dip by demanding payment from hundreds of companies who sent text messages to those very same licensed cells phones.

Helferich’s letters told its end user targets that companies that paid up immediately would get a discounted rate but threatened that this rate would go up if the target didn’t pay up within 60 days.

Numerous companies entered into licenses, but the New York Times and others decided to fight back. In the New York Times case, the District Court found that the original license to the cell phone manufacturers meant that no further license to the users was needed. And just last the month the USPTO cancelled one of the patents after finding it to be invalid in an inter

partes review.

We can only hope that Helferich was exaggerating when it claimed that over 100 companies already had signed licenses that it turned out none of the companies needed.

USEI

Another example is an entity called United States Ethernet Innovations, LLC (“USEI”). USEI purchased a group of patents that were about to expire from 3Com prior to 3Com’s acquisition by Hewlett-Packard.

In addition to filing numerous lawsuits, USEI has sent licensing threat letters to hundreds (or possibly thousands) of end user businesses. USEI’s letters assert that Ethernet technology is covered by their patents and their technology “is utilized in many day-to-day business activities within corporations, including internet connections, data transmission, retail transactions, corporate transactions, networked security system cameras, point of sale information, and inventory management systems.”

The letters further warn that USEI has hired “the largest and most successful plaintiff’s law firm in the world” and has recently filed infringement lawsuits, but that it was willing to offer a license to a “select group” of entities such as the letter target in order to avoid “protracted litigation.”

We understand that USEI has refused to provide its targets with information that would help them determine whether they actually need a license. For example, we understand that USEI has refused to disclose to its targets what entities already are licensed, a disclosure that would allow the target to determine whether the products it was using already were licensed and thus for which the target user did not have to pay. Targets of USEI's licensing campaign have included department stores, markets and other end user businesses both large and small.

Cisco's customers have received licensing demands from many of these shake down campaigns. In each case, the campaigns are inherently deceptive. The patents are often invalid or irrelevant to their targets or already licensed. The target end-users do not get a real picture of the licensing history and the real likelihood of suit. The massive deceptive letter writing campaigns are just a way for the scam artists to get far more money than their patents are worth (if they are worth anything at all) just like in any other scam.

Recommendations

Much of what we have said here is based on Cisco's own experiences and what Cisco's own customers have told us about their experiences.

But we do not know the scope and extent of the deceptive practices in which these entities are engaging. Our customers, the end user consumers that these entities are targeting and which we are seeking to protect, know even less. That is why your help is needed.

There are four simple steps that would make it much harder for these scam artists to use deceptive letter writing schemes to extract money to which they are not entitled from end user/consumer targets:⁷

First, require anyone sending patent demand letters to more than ten entities who are NOT the manufacturers of the accused products to file the letters in an on-line registry to be maintained by the FTC. The public, the targets of the campaigns and the FTC need to know the full picture.

Second, require anyone in that category to include in the letter a list of products which are deemed to infringe, including the manufacturer and model number, and informing them that they may have the right to have the manufacturer defend the case, and providing contact information for the manufacturer.

⁷ My proposal is very consistent with the White House's recommendations for reforming the patent system. See *Fact Sheet: White House Task Force on High -Tech Patent Issues (June 4, 2013)*, available at <http://www.whitehouse.gov/the-press-office/2013/06/04/fact-sheet-white-house-task-force-high-tech-patent-issues> (last visited April 3 2014).

Third, require any such letter to include the names of the entities which own the patents or benefit from their enforcement and any related entities.

And fourth, require the letters to include a list of all previous licenses granted for those patents, with a notice that if the recipient of the letter is using the products or services of a licensed entity, the recipient may require no further rights or permission from the patent holder. Also, the letter should say if there is a relevant licensing commitment to a standards organization.

By adding a basic level of transparency and accountability, these simple steps will help protect innocent end users.

The paycheck I get every other week says "Cisco" on it, but every cent comes from my customers. That is why I am passionate about making sure my customers who trust us to supply them with products don't get ripped off by these predators.

And when these predators are forced to come to me, I can guarantee they will get a fair fight.

Thank you. Please let me know if you have any questions.

Mr. TERRY. Thank you.

Dr. Dixon, you are now recognized for your 5 minutes.

STATEMENT OF MICHAEL DIXON

Mr. DIXON. Thank you, Chairman Terry, Ranking Member Schakowsky, and members of the subcommittee. I appreciate the opportunity to come here today. My name is Michael Dixon. I am president and CEO of UNeMed Corporation. We are the technology transfer and commercialization entity for the University of Nebraska Medical Center, so my testimony today will focus on preventing illegitimate and deceptive patent demand letters without modifying the U.S. patent system, or restricting university technology transfer offices.

Universities are uniquely positioned here because we work with innovators at the university level, as well as downstream partners that are trying to commercialize our discoveries. I am going to have three main points today. One, universities have an enormous economic impact. Two, strong and forceful patents must be preserved. And three, ambiguous, vague patent demand letters are the lifeblood of patent trolls, and using a tool like the FTC makes much more sense than modifying patent law for a second time in two years.

I would like to start by offering a bit of background on the scope of the University of Nebraska research and technology transfer. We are a proud member of the Big Ten, and have a very active research enterprise. Over the last 3 years we have invested \$1.1 billion in research. Three quarters of that funding comes from Federal sources, such as NIH, NSF, and DOD. In that time, 625 new inventions were created, and that led to more than 150 licenses to companies. So that is 150 companies that are going to invest more money to bring these discoveries to life, and make the world a better place.

Furthermore, 20 of those companies were created in Nebraska, creating economic development and jobs for Nebraskans in high growth, valuable companies. This licensing generated more than \$37 million in revenue for the University of Nebraska, and that mean more money for research, and more discoveries. Now, we are just one of many universities that undertake this. Last year, as a total, U.S. universities filed over 22,000 patents. They executed more than 5,000 licensing agreements, and generated \$2.6 billion in revenue. According to the Association for University Technology Managers, they added \$385 billion to the U.S. GDP. This is a very big economic force.

The economic impact is primarily based on patents. Companies are only interested in investing the millions or billions of dollars to bring these technologies to market if there is strong patent protection available. Quick story from our med center, as I mention in the testimony, the LeVeen needle electrode was invented at UNMC, and our industrial partner, Boston Scientific, brought it to the market. However, as the product neared FDA clearance, they found that it was necessary to enforce the licensed product against competitors. The parties both followed the appropriate protocol, worked out their differences through a patent infringement suit.

At the end, there was a cross-license, some payments, and the products were successfully brought to the marketplace. The system worked appropriately. The take-home message here is that any action must preserve patent rights, and to continue to provide incentives for both large and small businesses that invest in technology that makes our lives better.

There is a common theme with patent demand letters, and that is ambiguity. We have heard it already, bad actors are trying to scare, deceive, inappropriately extort money under the guise of patent enforcement, and they often use a shotgun approach, peppering the industry with hundreds of letters, often lacking in detail. As a technology transfer office, not only do we work with startup companies who have received these letters, but we have also been on the other side, and we have had to enforce our patent rights. When we make that important decision to send a demand letter, we find it is critical to provide detailed information for the recipient. In addition to a reasonable standard, it allows the recipient to make informed decisions.

In my written testimony, I offered seven items that we have in a demand letter. Items three through seven of this are often missing, as we have heard before, in demand letters. And I will say that, as a university, we are very conservative. We don't take litigation lightly. When we send a demand letter, we are going to go do our homework. And so, for us, it is very important that the recipient know what claims they are infringing, and that we identify specifically what product it is that is infringing those claims.

We want to make sure that the recipient knows who is suing them. Again, legitimate organizations don't hide behind shadow entities. If someone is infringing our patent, we want them to know who we are, and what our patent claims. Our goal is to settle the disagreement and provide as much information as is critical for that to occur. Some trolls use marketing entities that have no subject matter expertise, and cannot answer simple questions relayed in the demand letter. This, coupled with a shell entity, leads to a series of deadends and frustration for small businesses with limited resources as expenses mount with no answers.

Another quick story from one of our partners. They received a demand letter from a patent troll last month. While the letter identified the patent being infringed, it did not give the owner of the patent, the role of the organization contacting the company, a knowledgeable point of contact, or adequate time to respond. In fact, the point of contact turned out to be a marketing firm that was just established to send these letters through a shell company. The take-home message here is reduce the ambiguity associated with patent demand letters, and you will reduce the power of the patent trolls.

Thank you very much for your time. I look forward to any questions.

[The prepared statement of Mr. Dixon follows:]

71

Statement of

Michael J. Dixon, Ph.D.

President and CEO, UNeMed

Before the

Subcommittee on Commerce, Manufacturing, and Trade

Committee on Energy and Commerce

United States House of Representatives

113th Congress, 2nd Session

April 8, 2014

“Trolling for a Solution: Ending Abusive Patent Demand Letters”

Introduction

Chairman Terry, Ranking Member Schakowsky and Members of the Subcommittee, thank you for the opportunity to discuss patent demand letters, an important issue for America's innovation economy. My name is Michael Dixon, and I am President and CEO of the UNeMed Corporation, the technology transfer and commercialization entity for the University of Nebraska Medical Center (UNMC) and its sister campus, the University of Nebraska at Omaha (UNO).

My testimony today focuses on preventing illegitimate and deceptive patent demand letters without unduly burdening the U. S. patent system or restricting technology transfer efforts by universities. Universities are uniquely positioned interacting with both inventors upstream and commercial partners downstream as innovations make their way from the laboratory to the marketplace.

UNeMed and the Technology Transfer Process

UNeMed improves healthcare by fostering innovation, advancing biomedical research and engaging entrepreneurs and industry to commercialize new technologies created at UNMC and UNO. Similar to many other university technology transfer offices, UNeMed has a large and diverse intellectual property portfolio of new discoveries that represent significant opportunities in biomedical and clinical technology areas such as biotechnology, therapeutics, diagnostics, and medical devices as well as information technology software and hardware.

Last year, the University of Nebraska Medical Center (UNMC) invested nearly \$128 million in research for development of products that improve healthcare and save lives. One such product developed at UNMC was the LeVeen Radiofrequency Ablation Probe, which was the first minimally invasive radiofrequency ablation tool used to treat solid cancer tumors. UNMC researchers Dr. Robert LeVeen and Dr. Randy Fox invented this surgical device which helped to establish the field of interventional oncology. UNeMed and UNMC were eventually able to partner with Boston Scientific to bring this product to market. As a result, thousands of patients' lives have been, and will be, significantly improved. Our experience at UNMC is mirrored at many other universities across the country.

Patent Certainty and the Role of Demand Letters

For inventions to reach the marketplace, they must have meaningful patent protection. Certainty in patent enforcement is necessary for a company to license the invention and invest significant sums. For biomedical innovations that often means millions or billions of dollars will be invested to bring the product to the marketplace. Our commercial partners depend on patent certainty and strong patent protection to justify the significant financial investments required to transform an invention into a product ready for the marketplace.

As a University technology licensing entity, we have a unique perspective since our downstream licensees have received patent demand letters and upstream, as the holder of patents, we occasionally must send demand letters. We deal with both ends of this issue.

However, before talking about demand letters in detail, it is important to note that there are two types of activities that may be considered demand letters: 1) letters marketing inventions seeking investment, and 2) letters with allegations of infringement seeking compensation. The first, marketing inventions to potential licensees, is one of the primary missions of university technology transfer offices. We feel strongly that such activity is not a demand letter and should not be impacted by legislation aimed at those seeking damages for patent infringement. As a university with a significant patent portfolio, every day we send letters and communications to established companies in an effort to convince them to license and invest in our innovations and technologies. If legislation to standardize patent demand letters is contemplated, it is important to consider the potential impact on the technology transfer process. If, in trying to curb illegitimate patent demand letters, the minimum standard for such a letter constrains the ability of universities to communicate licensing opportunities to potential licensees, a university's ability to transfer technology into the private sector could be greatly harmed. Overly broad federal regulation would hinder legitimate efforts to market and license inventions on their journey to the marketplace.

Vague Demand Letters Stall Innovation

Of course, universities not only solicit partners for inventions. We also work with our partners to enforce our property rights and occasionally are also the target of demand letters. Universities and our licensees are negatively impacted by vague, overly aggressive demand letters. These demand letters seek financial gain through intimidation rather than legitimate patent enforcement. They are like rocks thrown in a stream which consume time and money, diverting and slowing the pace of innovations to the marketplace.

According to a 2013 survey by the American Intellectual Property Law Association, the cost of a patent infringement lawsuit for demands of \$1 million dollars or less averages \$970,000 to take the case to final decision (not including appeals). Just taking the case to the end of discovery phase still costs \$530,000. The potential financial risk inherent in patent infringement lawsuits, leaves most legal remedies out of reach for small businesses and inventors who receive a demand letter. For many, a wise business decision is to settle and move on, which further encourages illegitimate demand letters sent in great volume by shadow entities.

As an example, a few months ago, a company with whom UNeMed works received FDA clearance for a device the company patented. Their next step would be to create marketing materials and begin sales of the device. However, almost immediately after receiving FDA clearance, they received a demand letter asserting patent infringement against the company's product and made legal claims without providing sufficient information to evaluate the accuracy of the infringement charge. Ominously the letter ended, "I will be calling you to discuss the forgoing." For a small company with a limited budget having just completed the arduous and expensive FDA process, the prospect of additional time and money to hire attorneys to trace the source of a demand letter and to determine its legitimacy, does not make good business sense. While this letter could be illegitimate, for a small company dependent on an innovation, it is not worth the risk to ignore it. Many companies make a rational decision to pay the demand to make the claim go away.

A Reasonable Standard for Demand Letters

As we consider the facts above, we must also be careful that the patent enforcement bar is not raised too high. If it is, patent infringers will no longer respect intellectual property. Such a watering down of patent rights could lead to companies reducing investments in new products or resorting to secrecy instead of disclosure. Reducing investment or disclosure would cause significant disruption in our innovation ecosystem.

We seek a balanced approach and respectfully ask the Committee to consider the established best practices used by university technology transfer offices when we send demand letters. We follow our own strict standard to write the demand letter in a manner that, if we received it, we would know what the demand is and to whom to respond. In our judgment, a patent demand letter should contain the following elements:

- Identify the patent being infringed.
- Identify the infringing product or activity being done by the infringer.
- Specify the claim(s) in the patent being infringed.
- Identify the owner of the patent.
- Explain the role of the entity contacting the infringer.
- Provide a knowledgeable point of contact for discussing options for resolution.
- State a follow-up time which allows the infringer time to seek counsel and consider options before taking any next steps.

Unfortunately, illegitimate patent demand letters that have caused so much confusion and concern among businesses and researchers often lack many of these essential elements. Their ambiguity and lack of key information are essential elements contributing to their power to extract significant financial concessions.

If all demand letters were held to a standard that required due diligence, patent owners would be more likely to carefully target specific infringers rather than blanket businesses with demand letters. Infringers would have a clear understanding of the claims asserted by the patent owner and the entity contacting them. This would maintain the legitimate role that patent demand letters have in the patent enforcement process while curbing excessive behavior by those seeking financial gain through deceptive practices.

A Balanced Approach

The Bayh-Dole Act, the 1980 legislation widely credited with creating the university technology transfer industry has paid tremendous dividends to the U.S. economy. A 2012 study by the Biotechnology Industry Organization (BIO) found that technology transfer from academia and other non-profit institutions added more than \$385 billion to the GDP of the United States and created more than three million jobs and 650 new companies between 1996 and 2010. In 2013

alone, U.S. universities executed over 5,000 licensing agreements and generated \$2.6 billion in licensing revenue.

The America Invents Act, the most comprehensive reform in patent law in over 60 years, was only fully implemented a little over a year ago. Many of the reforms in this new law were targeted to eliminate overly broad low quality patents. More recently, the President directed the United States Patent and Trademark Office to take additional specific measures to address overly broad low quality patents. Changes are happening, but they will take time. Just as the Bayh-Dole Act has yielded tremendous returns over time, the America Invents Act and the changes in the courts and Administration should be given some time to achieve the intended purposes before additional burdens are placed on patent holders. Over time, these activities will reduce the number of questionable patents and reduce the incentives for illegitimate financial gain.

I applaud the Committee for exploring this issue, as there are still issues to be addressed, but I urge the Committee to take a balanced approach and be cognizant of the possibility of overcorrection. Universities are uniquely positioned interacting with both inventors upstream and commercial partners downstream as innovations make their way from the laboratory to the marketplace. America's universities are interested in continuing to work with you to ensure that the American innovation system remains the best in the world.

Thank you Chairman Terry, Ranking Member Schakowsky, and Committee members for the opportunity to offer my perspective to the Subcommittee. I welcome any questions you have.

Mr. TERRY. Thank you very much. And, I am sorry, Ranking Member Schakowsky has a meeting, so we are going to let her go out of order and ask the first set of questions. So, Ms. Schakowsky, you are now recognized for your 5 minutes.

Ms. SCHAKOWSKY. I appreciate that, Mr. Chairman. Is there anyone on the panel who thinks that it would be inappropriate for Federal legislation, not getting into specifics, is there anybody who thinks that Federal legislation is unnecessary? OK.

Attorney General Sorrell, you made a point of mentioning the issue of pre-emption in your testimony. I wondered if you could talk about that, though, on protecting whatever states do.

Mr. SORRELL. We are currently in litigation under our state Consumer Protection Act for unfair and deceptive acts and practices in commerce against this MPHJ Technology Investment LLC. And as soon as we filed that action under our so-called UDAP statute, MPHJ removed the case to Federal Court, and promptly said two things. One, that since this was in the patent arena that the lawsuit is not only frivolous, and filed for political purposes, but that we are totally pre-empted because patents are exclusively within the province of the Federal government, and, secondarily, that we lack personal jurisdiction over them for simply asserting patent infringement by sending these letters.

And that is why we are asking the Congress, if the Congress takes action here, to state clearly that AGs have legitimate—they are not pre-empted when there are unfair and deceptive acts and practices in the guise of an assertion of patent infringement, and that states are able to, without being pre-empted, enact statutes that prohibit bad faith assertions of patent infringement. So we are fighting that in Federal Court, U.S. District Court, in Vermont right now. And, given the fact that Nebraska, Minnesota, New York have already—

Ms. SCHAKOWSKY. You said Wisconsin?

Mr. SORRELL. Wisconsin hasn't yet, but Wisconsin has just enacted a statute on bad faith assertions of patent infringement, but the AGs of those other states have taken action, and in virtually each case been run up against this argument, you don't have any business here, you are pre-empted, because this is patent—

Ms. SCHAKOWSKY. Forty-two AGs you said, right?

Mr. SORRELL. Forty-two AGs signed a letter to Senate leadership about matters that are, actually just this week, moving forward in the Senate.

Ms. SCHAKOWSKY. OK. Let me just go through a list of things we have heard from a number of you, things that should be in these letters, in the demand letters. If anyone thinks that they should not be in a demand letter, let me know. Raise your hand. Identification of the patent being infringed, identification of the owner of the patent, contact information for a person who can discuss resolution, identification of each claim of the patent being infringed, identification of the infringing device, method, or service. OK, which one was that? Identification of each claim?

Mr. SKARVAN. Yes, identification—

Ms. SCHAKOWSKY. OK.

Mr. SKARVAN [continuing]. Of each claim. I think it was referred to earlier that, certainly, on behalf of the 21C, a number of the

members have extremely large equipment not readily accessible. Information is not readily accessible regarding that piece of equipment. We usually rely on trade shows, and perhaps advertising, regarding certain features, or possible benefits that seem to look like something we have a patent on. So when I am asked to provide analysis, or identify a claim against a product, I simply can't comply with that level of detail. I am not in possession of that information.

Ms. SCHAKOWSKY. OK. It is on the record. Thank you. Identification of the infringing device, method, or service, a description of how the device, method, or service infringes, identification of entities, other than the patent owner, who may benefit from enforcement, identification of all entities that had been granted—go ahead.

Mr. SKARVAN. I think you just have to be clear, when you talk about benefit from enforcement, that, I think, this additional detail is forthcoming, because there have been a number of proposals talking about how to identify that. Ultimately you are looking for somebody that, you know, in a lawsuit, their damages, if there is a fee paid, they would take and participate in that reward.

Ms. SCHAKOWSKY. Identification of the parent company of the patent.

Mr. SKARVAN. I will say, the devil is in the details. On the face, that looks simple. I have heard other companies state, for example, Intellectual Property Owners' Organization, that that in itself can be difficult to ascertain and provide correctly.

Ms. SCHAKOWSKY. OK. Identification of all entities that have been granted a license to the patent.

Mr. SKARVAN. Again, I think you start to get into a little bit of a burdensome situation with a company with tens of thousands of patents to understand exactly the entire licensing spectrum regarding that patent.

Ms. SCHAKOWSKY. OK.

Mr. DIXON. Also, on that one, I will say, from the university standpoint—

Ms. SCHAKOWSKY. OK.

Mr. DIXON [continuing]. If you are looking at non-exclusive licensing, sometimes those lists get very long, and sometimes a company's trade practices, they request some confidentially that they, in license, that technology for competitive advantages. So that may become a little difficult.

Ms. SCHAKOWSKY. OK. This is helpful. Notice to the recipient that they may have the right to have the manufacturer defend the case.

Mr. SKARVAN. I am sorry, could you repeat that?

Ms. SCHAKOWSKY. Notice to the recipient that they may have the right to have the manufacturer defend the case. And, last, some factual basis for the licensing fee, or settlement amount demanded, if any.

Mr. SKARVAN. Well, again, I come back to, I think, the very basic elements. These all require additional, I think, discussion and explanation, because these concepts can be very complex. I think when you come to the very basic elements that should be the content of a patent communication representing a demand on some-

thing, the identity a person or entity with a right to enforce the patent or patents forming the base of the demand, and identification with at least one product, service, or technology. Those, I think, are the key elements. When you add to those elements, I think you are getting into some very definitional and perhaps burdensome, complex disclosures that, really, at the point in time, are benefitting the assertion.

Ms. SCHAKOWSKY. OK. My time is expired. I appreciate that. So, we can inquire among all of you in writing responses to these suggestions, or just proposals. Yes. Thank you. I hear you on the burdensome issue.

Mr. TERRY. All right. Well, first of all, I think the nature of Ms. Schakowsky's questions were pretty similar to what I was going to ask, but it shows that if we are going to do, and I would say it is likely that we would draft something sometime in the near future. What we are trying to figure out is what, if we draft a bill, needs to be in there, and it appears to us that we need to itemize, or be prescriptive, in what has to be in a demand letter. So that is why Ms. Schakowsky did a list of things that have been discussed that should be in there.

Let me ask you just more generally, starting with you, Mr. Sorrell, or AG Sorrell, what are the characteristics that should be in a valid patent demand letter?

Mr. SORRELL. It shouldn't be any question of who is asserting the infringement. There should be evidence of investigation, or in depth analysis of this particular recipient's use of the technology that is allegedly violative of the patent. It should be clear if there are others with an interest in this assertion of patent infringement, and who they are. There should be legitimate addresses, contact information, for those asserting the infringement. If this patent has been the subject of a final decision, administrative decision, or a judicial case against the patent that is being asserted, that information should be reflected, at least for starters, and the demand should give a reasonable amount of time for the person to respond. And there shouldn't be this undue burden thrown to the recipient of a letter to prove your innocence, if you will.

Mr. TERRY. Right. As quickly as possible, Mr. Brouillard—

Mr. BROUILLARD. Yes, sir.

Mr. TERRY [continuing]. What points should be in a demand letter?

Mr. BROUILLARD. I would agree. I think it is obvious you can't receive a letter that simply says, A, we did an investigation, and found that you used our technology, and here is a list of numbers. It needs to be clearly identified as to what is being asserted, what investigation was conducted, how do you know that we are violating your patents? And, obviously, for someone like myself, who is totally ignorant of this issue until this all came up about a year and a half ago, there has to be something more than simply a list of numbers. To me, I don't even know if those numbers were legitimate patent numbers.

Mr. TERRY. OK. More—

Mr. BROUILLARD. More specificity in the claims that are being made.

Mr. TERRY. Mr. Skarvan, I am going to ask you the same question, but ask a little bit more clarity, because it does seem like you can identify what is being infringed. If you saw something at a trade show or an advertisement, you at least have a pretty good hunch that there may be an infringement. So it——

Mr. SKARVAN. I can suspect, because I obviously can't see inside, and I am stuck with advertising. I do want to bring up a point that we discussed a few things, and I want to differentiate a bit, if you don't mind, the difference between business-to-business communications, and the egregious actions I have heard here were end-users that are being targeted. And I will just say, in business-to-business communications, and patent demand letters, I think, generally under the law, the way it plays out, less is more, and let me explain that.

The number one concern prior to all this legislation that I had when I sent out a patent demand letter, or any member of the 21C sends out a patent demand letter, is does that contain enough information that the recipient feels immediately threatened, and they now have potential jurisdiction, they call it declaratory judgment jurisdiction, to say, look, this entity has threatened me. I cannot continue on with my investment without some certainty here on this issue. They brought the threat, I want it determined now. And all of a sudden you are in a patent lawsuit under what they call a DJ action.

And so when we send out letters, they tend to be a first in a series of letters. And when people point to a specific patent demand letter, all I can think of is, I have a series of letters to go out, none of them are the same. And they generally have these three things, but they don't have to, because I have different target audiences I am sending this letter to. So I just want to make sure that this kind of correspondence, which I think less is more, keeping it out of the courts, doesn't include a lot of these details.

And so, in answer to your question, I don't always have access to the information. I don't have that detail, nor may I want to even put that level of detail or threat in my letter if it ends up inviting a DJ action, and brings a patent suit in court.

Mr. TERRY. All right. The other three witnesses probably will have to submit that answer in writing, and I apologize that my time has run out.

So, at this point, Mr. Welch, you are recognized for 2 ½ minutes. No, Mr. McNerney, you are recognized for 5 minutes.

Mr. MCNERNEY. Thank you for the full 5 minutes, Mr. Chairman. I think it was really good testimony. I thank you all for coming this morning. One of the things that I think was a matter of disagreement among the witnesses is how to enforce this. I mean, there is a pretty good agreement that the letters should have a degree of specificity, but, as Congress, can we write a law that is flexible enough that it will be effective, that the patent trolls won't be able to get around, and so on, or should invest the FTC with the authority to do that in a way that would be effective?

Mr. Dixon, I think you had mentioned that you thought the FTC. How would we empower them, or do you believe they already have enough authority in the existing statute?

Mr. DIXON. I believe the FTC does have some authority here, and it would be wise of Congress to remind them that they do have some authority on some unfair trade practices. I think giving a little more teeth to the FTC, and allowing them to look at these broad, vague patent demand letters, while still, I agree, allowing business to business communications to still occur, and for business to transact that way, and not having that fall under this FTC action, is very important. But I think giving them a little more authority would allow business to still go on, and for these legitimate actions to still take place, while not affecting general patent law itself, which is the lifeblood of many of our businesses.

Mr. MCNERNEY. OK. Mr. Chandler, would you like to comment on that?

Mr. CHANDLER. Yes. I would make one distinction. Mr. Skarvan referred to business-to-business, and I think what we are referring to here is letters addressed to end-users. The end-users may, in fact, be small businesses, and I am not sure that some of the issues that Mr. Skarvan had with some of Ranking Member Schakowsky's enumerated proposals would apply in the case of an end-user communication, as opposed to when you are dealing with a competitor who is also a manufacturer, and where you have this dance that goes on in dealing with potential infringement allegations.

In looking at the end-user situation, I think the space where Federal legislation would be very helpful would be to establish clearly that it is an unfair business practice, in those types of communications to end-users, to not include certain types of information.

The FTC today can go after egregious misbehavers who are misleading and deceptive, but once you set a very clear set of standards, and also require transparency on those letters, manufacturers like me can step in. It almost becomes self-enforcing once you put some sunshine on these activities. And that is why there is a great opportunity to get something done here without creating a regulatory structure around it. What is really needed is daylight.

Mr. MCNERNEY. So you feel that Cisco can do a good job in defending your customers, if you have the right tools to do that?

Mr. CHANDLER. If we know this is going on, we can step in and do it. And if it is visible what is going on, these people will be forced to stop because the group of people who are being attacked can also band together and take action, as Mr. Brouillard has pointed out. But sometimes it takes some daylight before you know that this is actually happening. So transparency is really almost a solution in itself here.

Mr. MCNERNEY. Thank you. Mr. Skarvan, one of the things you recommended was that sanctions be imposed on bad actors. Wouldn't it be just easy for them, a bad actor, to put up another banner and continue on? Even though the first label is sanctioned, they can go to another label and carry on their activities?

Mr. SKARVAN. Well, I think what you stated is correct. It is very, very difficult to capture some of these actors, and I think it is very difficult in capturing them with a single demand letter that does or does not meet, if you want to say, the requirements set forth in legislation. What I think works more effectively is to capture their behavior. And the behavior we are seeing, I think it has been said

today, is that these hundreds and thousands of letters go to end-users.

And that is where you have got to really focus in on, and begin asking questions, because now you have got the behavior, and the business model I think people here are objecting to, these hundreds and thousands, I think it was 16,000—

Mr. MCNERNEY. Yes.

Mr. SKARVAN [continuing]. Letters nationwide. And that is where I think the FTC, uniform laws, and certainly uniform enforcement by the Attorney General, they act as a clearing house to identify this rampant behavior. And once you can see that behavior, now I think it is pretty easy to begin the inquiry into the entities engaging in that behavior.

Mr. MCNERNEY. Thank you. Thank you, Mr. Chairman.

Mr. TERRY. Thank you. Now recognize Vice Chairman of the Committee, Mr. Leonard Lance. You are recognized for 5 minutes.

Mr. LANCE. Thank you, Mr. Chairman. As I understand it, there are five or so existing state laws on this issue, and several other bills are awaiting signature by a governor, and there are as many as 19 bills pending in state legislatures. Given this situation, I would be interested in the panel's view as to whether Federal legislation is needed. Attorney General?

Mr. SORRELL. Yes, Federal legislation is needed, and hopefully included in that legislation would be an express statement that the states are allowed to enact their own statutes against bad faith assertions of patent infringement, and/or to enforce their standard Consumer Protection Acts.

Mr. LANCE. Thank you. Others on the panel?

Mr. BROUILLARD. Yes, I agree. I think that U.S. patent law is Federal legislation, and I think that anything that can be done to strengthen that legislation should be. In addition, I think to get back at the Congressman from California's comment, it is going to take a concerted effort on both the Federal and state level, in some cases, to do that. And the last point I would make is that if you had Federal legislation, then it is more uniform across all states, rather than a hodgepodge for companies that operate in multi-states to try to deal with.

Mr. LANCE. Thank you. Others on the panel?

Mr. SKARVAN. And I agree, and I am glad you brought that up, because not only is Federal legislation needed, but we need uniform legislation that provides the same, if you want to say, rules of the road across the states. States certainly can enforce through the AG, but as far as having different state statutes to provide different rules of the road, different, if you want to say, private causes of action, some have safe harbor, some have no safe harbor. I mean, looking for a little bit more uniformity.

Mr. LANCE. Thank you.

Mr. SCHULTZ. I would like to just add two things. One is that the patent system is an incentive system, and the Congress is in a great position to sort of balance those incentives. So if you want patent owners to do more to make sure that certain recipients get the information they need, you are giving them a patent, and you can require them to do things. I think that is a nice balance there that doesn't preclude states, but it kind of gives you that power.

The other thing is this bottom-feeder model, this model where they just send out thousands of letters, is premised on the idea that they don't have to be specific to the individual recipient, and I think that really needs to be in there someone, that core specificity, else they will just re-draft the letter in some other way.

Mr. LANCE. Thank you. Others on the panel?

Mr. Skarvan, you referenced safe harbor language in your comments, and in your testimony you suggest that safe harbor language be included. Do you have a specific idea what type of model you would like regarding safe harbor? Is there a provision in one of the state statutes that we might examine, and, if not, what would be an appropriate safe harbor provision, from your perspective?

Mr. SKARVAN. I think the most recent state that enacted a safe harbor, and worked through some of the language difference, was Illinois—

Mr. LANCE. Illinois, yes.

Mr. SKARVAN [continuing]. Statute, and when you look at the safe harbor, I think it is helpful to look at it in combination with the cause of action being limited to those letters sent to the end-users, and—

Mr. LANCE. Yes.

Mr. SKARVAN [continuing]. Have a good definition for end-users, including businesses, not for resale, in that statute. And they also have, not the subjective fact, but very clear false behaviors, along with very clear requirements of the patent owner, the patent number, and the general product or service it covers.

Mr. LANCE. So, from your perspective, we might examine the Illinois provision as a model for a Federal provision?

Mr. SKARVAN. Yes. We have suggested that to other states.

Mr. LANCE. Thank you. Others on the panel on whether there should be a safe harbor provision, and if so, what it should look like? No? Thank you, Mr. Chairman. I yield back the 37 seconds.

Mr. TERRY. Thank you. At this time I recognize gentleman from Vermont to ask questions to another gentleman from Vermont—

Mr. WELCH. Well, and others as well.

Mr. TERRY [continuing]. Mr. Welch.

Mr. WELCH. Thank you. I actually wanted to start with Professor Schultz. What options does a small business or startup company currently have when they receive one of these vague threatening demand letters?

Mr. SCHULTZ. So I think that, if they are taking a rational approach, they want to think about this as, you know, first, as we doing what they say? Are we infringing some patent? And then they have a couple of options. One is they can challenge that assertion, right, in that they can get an attorney, if they could afford one, or get pro bono counsel.

The second is they can decide to change what they are doing, or design around that, and that is where the specificity really helps them. If they realize that it is only one small piece of whatever they are designing or doing, they can maybe change that, and then maybe settle a little bit, but move forward.

And then the third is they can simply just pay to get out of the way, which what so many of these are doing. So I think we want

to give them valid choices, and the only way to do that is to have the specific information.

Mr. WELCH. And then what is a remedy if there is an absence of specificity?

Mr. SCHULTZ. You mean in terms of what?

Mr. WELCH. For the receiver of that letter.

Mr. SCHULTZ. I mean, they are really stuck in a kind of quandary, because they don't know what to do. They can't explore those other choices. They don't know how to change what they are doing. They don't know whether to challenge it, because the allegations aren't there, so the only rational choice left is to pay off the sender.

Mr. WELCH. OK. I want to go back to Mr. Sorrell, and have you think about this question too, because I might want to get your point of view. But you have been really advocating that this is a consumer protection issue, and that there has to be some role for the states, and it would be a mistake for the Federal government to pre-empt. Just elaborate on that a little bit.

Mr. SORRELL. These efforts are so widespread that there is plenty of work for both Federal regulators and state regulators. If you look at it from the drug trafficking analogy, the Federal authorities typically take, you know, the cartels and the large dealers, and they leave the street dealers to the states. If we are looking at assertions of pattern infringement, I believe the FTC does have authority, but it can't police this spectrum entirely, and there is a role for the states.

Mr. WELCH. Professor Schultz, do you think that makes sense, in terms of a practical way to protect innocent victims, like the Lincoln Street example? You know, a small nonprofit, and those options you laid out, I think for them, mainly, they are just terrified, and they can't make that phone call to the lawyer because they know the meter is running once that happens. And they hope it goes away, and it doesn't.

So it seems to me that what General Sorrell is suggesting, that there be a consumer protection element, a local ability of local consumer protection division, and an Attorney General's office closer to the scene to be able to protect, I should say, the rights of some of these small businesses.

Mr. SCHULTZ. Absolutely. I think that is an essential component. But I do think that, since the patent law is Federal, it is also worth looking at the incentive systems, and allowing the option that you could provide consequences in the Federal system too. Because—

Mr. WELCH. Right.

Mr. SCHULTZ [continuing]. Some of these things do go to court, and when they go to court, there are consequences to whether the letter was sent, and what it said.

Mr. WELCH. So if we provided consequences at the Federal level, I mean, I like what you are saying about the incentives, that makes a lot of sense to me, would we want the benefit of local enforcement of those standards that we have established here at the Federal level?

Mr. SCHULTZ. Absolutely. I think both can coexist, and, in fact, contribute to the same goal.

Mr. WELCH. OK. By the way, do patent holders, I will stay with you, Professor Schultz, other than the trolls, routinely target end-

users, and could there be any legitimate reasons to send demand letters to end-users?

Mr. SCHULTZ. So I will say generally no, except that this term end-user, I think we have to be careful, because these are very clever lawyers, right, who run these companies, these trolls. And so if you define something too specifically, in terms of one protected group, you know, they will try and find a way around it.

So I just want to be careful, because, again, a lot of the folks who call my clinic, and are looking for pro bono assistance, are people who develop apps. And they are, like, two or three small, you know, it is a small business, two, three people, just trying to create something to put on the iTunes or Google store, or whatever. They are not end-users in a sense, except they are the end-users of the Internet.

Mr. WELCH. Yes.

Mr. SCHULTZ. Right. So I just want make sure that if we are going to cover people who are using standard technology, it is not just only the physical stores, but it is also anyone who kind of is using a product or service from someone else.

Mr. WELCH. So I will ask the whole panel, is there—I have only got 18 seconds.

Mr. TERRY. Yes.

Mr. WELCH. Well, I guess I won't. Well, the question I was going to ask, but then I will yield before there is an answer, is what evidence do we have about the effect of patent trolls on suppressing innovation?

Mr. TERRY. All right. That would be a great answer for a written question—

Mr. WELCH. All right.

Mr. TERRY [continuing]. That we will submit. At this time—

Mr. WELCH. I yield back.

Mr. TERRY. Thank you. Gentleman yields back. Recognize the gentleman from Texas, Mr. Olson, for 5 minutes.

Mr. OLSON. I thank the Chair. And, first of all, I don't like the term patent trolls. These aren't patent trolls. They are patent bullies, like the bully on the playground in 3rd grade, the bully every Monday who comes to school, threatens to beat you up if you don't give him his lunch. I mean, these are patent bullies.

And, thinking out of the box on how we stop this behavior, in my home State of Texas, again, not directly applicable, but they did something in 2011 called basically loser pay. My state Senator, Joan Huffamn, got that thing passed. It has been going on for about 3 years now, and what they have done, not so much, again, in patent protection, but just sort of legal protections for some of these frivolous lawsuits, they basically empowered the judge, the trial judge, to say, this is garbage, throw it out. He gets the initial filing, say, frivolous, done.

If that doesn't work, OK, how about I send it up to—they are going for the home run. We know it is really bad, but we want to take that shot, maybe knock that thing out of the park. And if that is the case, I can send it straight from my court to the Appellate Court, get this taken care of quickly, so, again, the aggrieved party is not paying legal bills on, and on, and on. Also, for the small

guys, it was less than \$100,000, you know, expedited civil action procedure.

And so, to ask all the panelists, is that something we should look at? I mean, I know there are lots of pros and cons, more Federal involvement, pre-emption, that type of stuff, but, again, how can we take this ham away from these patent bullies, not patent trolls?

Mr. BROUILLARD. If you don't mind, I will take the first shot at it. I certainly believe that part of the legislation should include some opportunity for the party that has been aggrieved in this situation to have their costs reimbursed. I suspect if I got a letter from Caterpillar, I would pay attention. But when I get a letter from an entity I don't know that just lists a whole bunch of numbers clearly, for someone like us, or any small business, to defend, we have been told it is a million dollar cost to defend a patent lawsuit. We are certainly not in a position to do that, and I really do believe that if a patent troll, or if a patent bully, ran the risk of having to reimburse someone, they would think twice about doing it in the first place.

Mr. OLSON. General Sorrel, any comments, sir? And my parents are voters in Vermont.

Mr. SORRELL. In the Vermont statute, it allows for awarding attorney's fees. But, again, to recover, you have to establish that there was a bad faith assertion of patent infringement. And I think some of the concern about AGs getting involved in this arena is, are we going to sort of muddy the waters?

Speaking for myself, and pretty comfortably for the rest of the AGs, we do not want to try to get in the middle of a fair fight between two companies, where it is a reasonable fight as to whether this patent exists, and what it controls. We are really trying to deal with the bottom-feeders, and we think that the current Federal standard of the awarding of fees in patent cases ought to be eased so that they are awarded more frequently. I am not prepared to say that the loser pays in every case. That might be an overreach there.

Mr. OLSON. Mr. Skarvan?

Mr. SKARVAN. Well, I would just say that some of these concepts, I think they can work, conceptually. Generally they fall down if you try to apply them just to one side of the coin, so they have to be available, similar to bonding, to both parties, because they are pre-determining that somebody actually is the bully ahead of time. It all comes down to what actually is going on. Certainly wouldn't want to be one-sided and attach that type of penalty to a legitimate patent communication.

Mr. OLSON. Yes, suddenly the bullied becomes the bully, maybe, in that situation.

Professor Schultz, any comment, sir?

Mr. SCHULTZ. Yes. So I do think that many of the efforts that are being supported in Congress right now, I think, are comprehensively looking at the problem, and I think that linking them together, and making sure they all fit well together, is good. So I think that, for instance, the type of demand letter, or the kind of information that is or is not shared, and how vague, and how deceptive it is may well be appropriate factors to pay into a fee award, right, or to say an adjustment of whether damages are available for willful infringement or not. These kind of things, I

think, are linked, and are important. But I do think that the whole problem needs to be dealt with on a couple different levels.

Mr. OLSON. OK. Mr. Chandler, I have got time, sir. You have got one more swing to take it out of the park?

Mr. CHANDLER. You know, the Innovation Act that passed the House with overwhelming bipartisan support includes a provision for some cost-bearing when a case is completely unreasonable. In this particular type of problem that we are talking about today, though, it is unclear how that plays out, because these things don't generally go to litigation, because they get settled, because you have someone who is using Wi-Fi in their business, and is told you can spend hundreds of thousands, or millions of dollars to defend this, or you can just pay us \$2,000. So I think——

Mr. OLSON. Yes, the bully.

Mr. CHANDLER [continuing]. The promise of that might be a looser rate. I don't call them trolls because I don't like to demonize my adversaries. I would just say they are like rats running through a maze, and we need to take the food away at the end, and then they will stop going through the maze. And that is a systemic issue that we can address that won't result in a lot of litigation and awards at the end.

Mr. OLSON. Thank you. My time restrictions are very brief, sir.

Mr. TERRY. Thank you——

Mr. OLSON. Mr. Chair——

Mr. TERRY [continuing]. Mr. Olson. Now recognize the gentleman from Illinois, Mr. Rush, for——

Mr. RUSH. Well, thank you, Mr. Chairman, and it has been quite interesting. I want to thank the witnesses for appearing before this subcommittee. Earlier, when Congressman McNerney asked about the FTC's authority, and Dr. Dixon mentioned that the FTC already has authority, and could be encouraged to use that authority. Perhaps, Mr. Chairman, we should encourage the FTC to be more aggressive on the issue of patent trolls, be they bullies, or rats, or however you want to define them.

However, I am interested in understanding what additional authorities the FTC could use in this space. For example, General Sorrell, the FTC does not have authority currently to collect civil penalties under Section V for unfair and deceptive practices. General Sorrell, shouldn't the FTC be able to bring cases for more than just injunction relief, and also hitting these bad actors, be they rats or trolls, directly in the pocketbook? And also, are there other authorities that would be helpful, such as ACA rulemaking, on declaring certain actions to be, "per se, deceptions"? For example, if a demand letter does not include the patent number, or numbers, couldn't they just be, based on that, declared, per se, deceptions? Or——

Mr. SORRELL. Thank you. In my view, the Federal Trade Commission does have authority in this arena right now, and that is in part evidenced by the fact that MPHJ Technology, that when the Federal Trade Commission started investigating MPHJ Technology, it turned right around and it sued the Federal Trade Commission to halt the investigation. That being said, I would suggest that there be a communication to the Federal Trade Commission about the other issues that you raised, whether they think that the

Congress might underscore or enhance the authority that they currently have.

My concern is that, if legislation just speaks to enhanced authority for the Federal Trade Commission, and you don't speak to the states' authority to enforce our statutes, it will be argued that you were consciously trying to cut the states out of the equation.

Mr. RUSH. And are there any other witnesses who want to comment on increasing the authority of the FTC? Mr. Chairman, thank you, I yield back.

Mr. TERRY. Thank you, Mr. Rush, and I appreciate your input. Now recognize the gentleman from Ohio, Mr. Johnson.

Mr. JOHNSON. Thank you, Mr. Chairman, and I appreciate the panel being with us today.

For all of you, and you can answer in whatever order you would like, what role should the Federal Trade Commission have regarding patent demand letters? Anybody want to comment?

Mr. SORRELL. I think I just answered that question, so I pass it down the line.

Mr. SCHULTZ. I will just add one thing, which is that I do think this question of understanding the problem, I think we have a pretty good handle on it, but I think, for instance, one of the questions is, what are the subpoena powers of the FTC, in terms of getting access to the letters that a particular entity might have sent out that they are not aware of, things like that. And I do think that, if we are going to support the FTC investigating, or state AGs as well, that they do need to understand the problem, and they do need to see the letters that have gone out, and the practices of the entities. So I think that information collection is an important aspect.

Mr. JOHNSON. OK. Mr. Chandler?

Mr. SKARVAN. Can I speak to the—

Mr. JOHNSON. I am sorry, go ahead, Mr. Skarvan, yes.

Mr. SKARVAN. Thank you. I speak to just the consistency and uniformity, and ensuring that consistency and uniformity, and providing that clearinghouse function to identify the bad behaviors, and giving comfort to the company that sends a handful of demand letters that they won't be brought into a private cause of action at the state level by perhaps a recipient who wants to play mischief.

Mr. JOHNSON. OK. Mr. Chandler?

Mr. CHANDLER. Thank you. I think the FTC has the authority today to go after, for unfair business practices, the most egregious cases. The opportunity that you have on legislating on this is to set some very, very clear standards for what a demand letter to end-user or a small app developer would have to include so that you have an immediate step that the commission can take to try to demand transparency.

So rather than creating a regulatory structure around the ultimate enforcement action for the underlying acts, by making very clear what a demand letter has to have, I think you stop automatically a lot of this activity, because these entities that are doing this can't stand to have the sunshine expose what is going on. And just setting that standard for needs to be in the letter I think will go a long way toward solving the problem itself.

Mr. JOHNSON. OK. Mr. Dixon, in your testimony you distinguished between letters with allegations of infringement seeking compensation, versus letters marketing inventions, seeking investment.

Mr. DIXON. Yes.

Mr. JOHNSON. How are these letters different from each other, and what do you say that distinguishes them? Or what do the letters say that distinguishes them?

Mr. DIXON. So I think this really gets back to the business communications that we would have as a university. When we are trying to market our technologies, we are trying to incentivize investment. But oftentimes within these letters, we are identifying intellectual property that we own, and we are letting a company know that they may be interested. For example, I have got a cancer vaccine. I know Eli Lilly works in cancer. I am going to send them a letter saying, would you be interested in developing this technology? I think the major difference here is that patent demand letters will contain the threats of litigation, and often require that license.

Now, as has been stated earlier, these trolls are very bright, and so one of the things, I think, that will be difficult is to craft the right legislation that will prevent the troll-like activity, while not stopping these typical business communications that are vital for us to continue on. Because universities and companies need to send letters to one another identifying potential IP that we might want to cross-license, or develop together, we want to make sure that that does not get caught in any sort of FTC regulation that slows the pace of innovation and development.

Mr. JOHNSON. OK. All right. Mr. Skarvan, you stated you want a safe harbor to preserve your rights to put companies on notice. What is the difference between the manner in which you communicate your patent rights, and the manner in which a patent troll communicates his alleged patent rights?

Mr. SKARVAN. Well, I think there is a whole spectrum of, again, using the word patent trolls, but maybe better word in sum of this, of using the patent demand system, or patent demand letter. I think any patent holder who is engaging in good faith communications is entitled to those safe harbor rights. When you start talking about an abuser, and somebody that is acting in bad faith, objectively bad faith, false statements, then that person is not entitled to those safe harbor rights, because they are not acting in good faith.

And so the difference really isn't so much the label of the person exercising the patent right, it is whether or not they have engaged in this abusive behavior. Then they are not entitled, because they have been acting in bad faith to those, if you want to say good faith rights that everybody has.

Mr. JOHNSON. OK. All right. Thank you, Mr. Chairman. My time has expired.

Mr. TERRY. Thank you. Now recognize the gentleman from Illinois, Mr. Kinzinger, for 5 minutes.

Mr. KINZINGER. Well, thank you, Mr. Chairman, and thanks for holding the hearing, and to all of you, thank you for coming out. Especially nice to see the folks from CAT here. It is a good home

state company. I am grateful for the panel's insight on these issues of the abusive patent demand letters. In my office, we have heard from several consumer groups, realtors, credit unions, and banks, and they share a common message, which is patent demand letters are often deceptive, confusing, and intimidating.

It is certainly concerning that some entities are purposely misusing patent demand letters. These tactics hurt job creation, hinder innovation, and place a significant financial toll on consumers, businesses, nonprofits, and other actors within the economy. As we consider these abusive tactics, as we have had a lot of discussion today, it is important to keep in mind that demand letters do serve a legitimate purpose in the patent system, and any reform should ensure legal patent holders' rights are protected. With these considerations in mind, I have a few questions I would like to ask.

I will start with Mr. Skarvan. You probably know the Illinois bill better than I do, but could you tell me any shortcomings that the Illinois bill has, and then where the Federal government would have a role in, in essence, pouring cement over that in order to protect the rights of companies?

Mr. SKARVAN. Shortcomings? I actually applaud Illinois for coming up and crafting a compromised solution.

Mr. KINZINGER. Well, I guess let me rephrase shortcomings. Instead of saying where would you believe that in Illinois the Federal government then would need to step in after Illinois has done what it has done?

Mr. SKARVAN. Well, looking at the Illinois language, if I am answering the question correctly, I would like to see any Federal legislation, any rules put in place, to be consistent with the Illinois language, because I think everybody agrees it is those communications that are sent widespread, hundreds and thousands to the end-users, that are clearly the abusive practices that people seem to be keying in on. So that language in the Illinois, I think, is pretty key, and I think people have mentioned that. Definitional language is important to understand that. And when questions have come up on the Illinois legislation it is—

Mr. KINZINGER. Right.

Mr. SKARVAN [continuing]. Usually around the definition of consumer, and person, and not for resale type language that is inherent in that bill.

Mr. KINZINGER. So, then, for the whole panel, with all your stakeholders, Illinois has its language, let us say Pennsylvania comes up with its language, Iowa comes up with its own, what is the concern with how you practice your craft, in terms of states that have all kinds of different languages not consistent with, for instance, Illinois, or no Federal provision? We could start on the very left, sir, if you want to go, if you guys have any thoughts on the varying state proposals.

Mr. SORRELL. The Vermont statute is for bad faith assertions of patent infringement. I am not familiar with the specifics of the Utah, Virginia, Oregon, and Wisconsin laws, nor the others that are being considered. But to the extent that the standard is bad faith, then I am not of the view that companies that make good faith assertions of patent infringement have a problem.

Mr. KINZINGER. OK.

Mr. BROUILLARD. Yes. Clearly, I think, from our point of view, patent law is Federal law. And so, as I mentioned earlier, I think it is important that there not be a hodgepodge of legislation at state level that starts to countermand things that would be good practices for companies that do operate on a multi-state, or multi-national basis, such as we have heard today from Caterpillar, and Cisco, and others.

Mr. KINZINGER. Yes. Mr. Skarvan, if you could talk to specifically how it would affect your company if you have varying state laws?

Mr. SKARVAN. Well, I actually asked that question specifically with the folks in my group, and with that wide variety, we literally have to have a spreadsheet to hang over your desk, and understand what states cover what, and what the penalties are. And, at the same time, you would have to have an understanding of exactly what states are in play, because, you know, many recipients in our line of business are multifaceted state participants. In the end, I think it would absolutely kill our ability to send out any communication.

And I just wanted to reinforce, there isn't a magical patent demand letter that suddenly appears at some point in time in the conversation between business to business. It is a series of communications where you are trying to invite dialogue, and trying to address this issue, and get more information, find out more, and move toward a solution, all outside the court system.

Mr. KINZINGER. Thanks. Thank you. And any of the other three gentlemen, I only have 40 seconds, if any of you three have anything to add, please do.

Mr. DIXON. I had a really quick comment. I think one of the dangers here is putting back on the states the requirement of determining what is legitimate and who is lying, because within this there is a pretty gray spectrum of entities that are maybe stretching what their patent claims may actually be, and so that is what the Federal Court system is designed for. And I agree, the bad faith need to be taken care of, but there becomes a gray zone, and we don't want the state Attorney Generals having to do patent claim charts all of a sudden.

Mr. KINZINGER. Right.

Mr. DIXON. We want that done in Federal Court.

Mr. KINZINGER. OK. With that, Mr. Chairman, thank you, I yield back.

Mr. TERRY. Thank you, Mr. Kinzinger, and we have no other witnesses, so I have to do a little business here before I can adjourn this. And so we have statements for the record, and I ask unanimous consent to insert into the record these papers and letters from Span Coalition, Credit Union National Association, Independent Community Bankers of America, National Association of Federal Credit Unions, and National Retail Federation. This has been vetted on both sides. So, hearing no objection, so ordered into the record.

And I want to thank all of you for being here. It was a very narrow, intellectual discussion, and I think it was a really good discussion, and very helpful to us. And I really appreciate all of your efforts and sacrifices to be here today to help us now, as we will sit

down and start figuring out how to draft a bill. You are now adjourned. Thank you.

[Whereupon, at 11:44 a.m., the subcommittee was adjourned.]

[Material submitted for inclusion in the record follows:]

April 8, 2013

The Honorable Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing and Trade
House Committee on Energy and Commerce
2125 Rayburn House Office Building
Washington, DC 20515

The Honorable Jan Schakowsky
Ranking Member
Subcommittee on Commerce,
Manufacturing and Trade
House Committee on Energy and Commerce
2322A Rayburn House Office Building
Washington, DC 20515

Dear Chairman Terry and Ranking Member Schakowsky:

We, the undersigned trade associations and members of the Stop Patent Abuse Now Coalition ("SPAN Coalition"), applaud bipartisan efforts moving through Congress to curb abusive patent litigation. As you know, The House passed HR 3309, *The Innovation Act*, in an overwhelming bipartisan vote of 325-91 on December 5, 2013. However, for jurisdictional reasons, the bill did not include comprehensive provisions to address vexatious pre-litigation demand letters. As Congress continues to consider patent litigation reform, we urge you to help develop provisions that would provide the FTC with further direction under its existing Section 5 authority to go after the unfair and deceptive pre-litigation demand letters that patent trolls routinely send to unsuspecting businesses and not-for-profits across the country.

As you heard in testimony given at the Subcommittee on Oversight and Investigations on November 14, 2013, and will hear again today in the Subcommittee on Commerce, Manufacturing and Trade, patent trolls are harassing businesses and not-for-profits of every size, across an increasingly wide swath of industries, with demand letters. These letters come out of nowhere, and often allege that the mere use of everyday technology violates the patent holders' rights. Further, these questionable letters typically state vague or hypothetical theories of infringement, often overstate or grossly reinterpret the patent in question, and, in some cases, make allegations of infringement of judicially invalidated, expired or previously licensed patents.

At their core, demand letters use the mere threat of litigation as leverage to extract a "licensing fee" from the recipient business. Recipients often simply settle these nuisance claims rather than run the risk of engaging in a complicated and protracted legal battle. Put simply, it is often much more expensive to hire a patent attorney to review or defend against a suspect claim than it is to pay the requested "fee." This is the troll's calculated business model.

Vague and misleading pre-litigation demand letters are at the very center of the patent troll problem. Many, if not most claims begin and end with a demand letter as companies quickly pay undeserved "licensing fees," to simply make the patent troll go away. We urge the subcommittee to pursue meaningful solutions to protect businesses of all sizes from these "smash and grab" tactics. The fight for patent litigation reform and demand letter relief is truly a main street issue impacting businesses and not-for-profits in communities across the country. We look forward to continuing to work with you on this important issue.

Sincerely,

National Retail Federation

American Association of Advertising Agencies

Direct Marketing Association

Association of National Advertisers



Bill Cheney
President & CEO

601 Pennsylvania Ave., NW
Sutton Building, Suite 600
Washington D.C. 20004-2601

Phone: 202-506-6745
Fax: 202-638-7734
b Cheney@cuna.org

April 7, 2014

The Honorable Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing and Trade
Committee on Energy and Commerce
United States House of Representatives
Washington, DC 20515

The Honorable Jan Schakowsky
Ranking Member
Subcommittee on Commerce,
Manufacturing and Trade
Committee on Energy and Commerce
United States House of Representatives
Washington, DC 20515

Dear Chairman Terry and Ranking Member Schakowsky:

On behalf of the Credit Union National Association (CUNA), I am writing to thank you for scheduling the Tuesday's hearing entitled, "Trolling for a Solution: Ending Abusive Patent Demand Letters." CUNA is the largest credit union advocacy organization in the United States, representing America's state and federally chartered credit unions and their 99 million members. We appreciate the opportunity to submit this letter for the record of the hearing.

Patent Assertion Entities, commonly referred to as "patent trolls," have targeted credit unions with demand letters claiming infringement on a broad range of obscure and vague patents. In some cases, the patents have already expired or been held invalid by courts. These demand letters are intentionally vague and target credit unions that may lack the legal expertise on staff to fight the claim, often resulting in quick settlements. The technologies for which patent demand letters and litigation have become common against credit unions include some of the things that make financial services most accessible to consumers – ATMs, online and mobile banking, remote check capture, and check processing.

These letter writing campaigns work because trolls know that an early settlement is much, much cheaper for a defendant than fighting. In almost every case, just to pick up the phone to consult a patent lawyer to determine the validity of the infringement claim and evaluate the demand costs tens of thousands of dollars. Credit unions are filled with staff in the business of managing risk, and in targeting small institutions that may not have a lawyer on staff competent to evaluate the claims, demand letters are sure to reach a captive mass of people who will be afraid of getting sued. Most credit unions will be willing to do almost anything to avoid the risk and uncertainty litigation creates.

As you look for solutions to address this growing problem, we ask that you consider provisions that increase transparency and strengthen disclosure requirements for demand

The Honorable Lee Terry
 The Honorable Jan Schakowsky
 April 7, 2014
 Page Two

letters, and clarify that the Federal Trade Commission (FTC) has enforcement authority over patent trolls that operate in unfair or deceptive ways. In the same way heightened pleading requirements can help keep frivolous lawsuits out of court, minimum disclosure standards would help ensure that only demand letters truly asserting a potentially valid claim of infringement are sent. The minimum standards of transparency could be established by Congress, or a federal agency through rulemaking, whether that agency is the FTC or Patent and Trademark Office (PTO).

In addition, we support the creation of a demand letter registry and a requirement on entities which sends more than 10 demand letters in a single calendar year to enter all letters into a registry. The registry should be publicly available and maintained by a federal agency, perhaps the PTO or FTC. Such a registry would facilitate the sharing of information among demand letter recipients and also provide law enforcement with the information necessary to conduct proceedings against abusive trolls. Moreover, it would reduce the intimidation factor associated with the demand letter scheme.

We encourage the Subcommittee to pursue this issue and these recommendations and would be happy to discuss this further at your convenience. On behalf of America's credit unions and their 99 million members, thank you very much for holding this hearing and considering our views.

Best regards,


 Bill Cheney
 President & CEO



April 8, 2014

Abusive patent infringement claims threaten community banks

On behalf of the Independent Community Bankers of America (ICBA) and the nearly 7,000 community banks we represent, thank you for convening this important subcommittee hearing entitled "Trolling for a Solution: Ending Abusive Patent Demand Letters." We appreciate the opportunity to put forth our views on the issue of abusive patent litigation brought by patent assertion entities (PAEs), popularly referred to as "patent trolls", which assert infringement of dubious-quality patents against legitimate businesses, including many community banks.

According to a 2012 study of the issue, direct costs associated with litigation brought by PAEs are substantial, totaling an estimated \$29 billion in accrued litigation and non-litigation costs in 2011.¹ Managing these aggressive and frivolous patent lawsuits has become an expensive distraction for an increasing number of community banks that often lack the financial and legal resources to properly dispute these claims and are forced to settle out of court. These claims and settlements sap valuable monetary, management and legal resources from community banks that would otherwise be directed toward serving the financial needs of their customers. What's more, PAEs use settlements to build war chests to target other legitimate small businesses. The business community at large² is looking to Congress to create effective tools to stop this vicious cycle.

ICBA commends the House of Representatives for passing H.R. 3309, the Innovation Act, earlier this year. H.R. 3309 contains several provisions to help constrain PAEs and is a strong first step but more needs to be done to address this growing issue. We look forward to working with members of the House Energy and Commerce Committee to identify ways to end these deceptive and destructive practices brought by PAEs.

Below, please find some suggested measures to protect community banks from the abuses perpetrated by PAEs.

Demand Letters

Community bankers across the country have seen a dramatic increase in the number of demand letters received from law firms representing PAEs. The typical letter states that the community bank is in violation of a patent or a suite of patents held by the PAE. Typically, the PAE is willing to settle or sell a sub-license, often a "limited or one-time offer," to the community bank for using the technology in question. These letters are often accompanied by a list of patent numbers issued by the PTO but contain no description of what the actual patents are or how the community bank is in violation. The community banker is then forced to choose between costly and time-consuming litigation to challenge the patent or compliance with the letter's demands, regardless of how dubious the infringement claims are. Compliance with the demand letter strengthens the PAE's incentive to target additional community banks to extract exorbitant and fraudulent fees. Furthermore, if a demand letter is ignored, a second more threatening letter

¹ The Direct Costs from NPE Disputes by James Bessen and Michael J. Meurer (Boston University School of Law) 6/22/12

² ICBA is a member of the Main Street Patent Coalition. The Main Coalition is a national, non-partisan coalition of organizations dedicated to stopping patent abuse from trolls by encouraging Congress to pass comprehensive, common sense patent reform legislation – now. <http://mainstreetpatents.org/page.asp?id=19>.

One Mission. Community Banks.

1615 I. Street NW, Suite 900, Washington, DC 20036 ■ 202-659-8111 ■ Fax 202-659-9216 ■ www.icba.org

is often issued along with a dramatic increase in the settlement or sub-licensing fee further illustrating the extortive nature of this act.

To address this issue, ICBA urges Congress to pursue legislation that would strengthen demand letter transparency. Each demand letter sent by a PAE should be detailed and personalized to each recipient and not sent "scatter-shot" to dozens of community banks in a given state. Each demand letter should provide a detailed description of the patent, including each claim of each patent that is allegedly infringed, as well as a detailed description of the alleged infringement. The letter should also disclose the actual owner of the patent and all relevant case history involving the patent.

Additionally, a PAE that sends more than 10 demand letters in a calendar year should be required to enter these letters and other detailed information regarding their patents and their assertions of infringement in a Federal database housed at the PTO or the Federal Trade Commission (FTC). This would increase transparency in an extremely murky area and allow those accused of infringement to identify other similarly situated businesses to enter into joint defense funds and pool valuable legal resources. This would also decrease the tool of intimidation used by PAEs by letting those that receive demand letters know that they are not alone in this process.

Demand letters are a considerable drain on a community bank's finite resources. Legislation that increases demand letter transparency would go a long way to helping community banks make informed decisions on whether to settle ("feed the troll") or to fight the claim through litigation.

End User Indemnification/Warranties

Community banks often white-label products that are purchased from vendors to serve their customers. Community banks are "end-users," not creators of these products and services and should not be on the hook for the infringement claims of PAEs. Community banks are especially vulnerable to being sued because they lack the resources and market power to fairly negotiate the protections they need when contracting with large sophisticated vendors. Additionally, the vendors that provide these products and services to community banks often do not stand behind them with regard to patent issues. As a result, when a community bank is accused of infringement, the vendor, often better situated to refute the claim, sits on the sidelines and refuses to defend its customers.

To address this problem, Congress should amend current law to ensure that vendors that sell products or services to community banks provide the appropriate warranties and indemnification to protect the end users from patent infringement claims.

Thank you again for convening this very important hearing. We look forward to working with this subcommittee to curb abusive patent infringement claims that threaten community banks and the customers and communities they serve.

One Mission. Community Banks.

1615 L Street NW, Suite 900, Washington, DC 20036 ■ 202-659-8111 ■ Fax 202-659-9216 ■ www.icba.org



3138 10th Street North
Arlington, VA 22201-2149
P: 703.842.2234
F: 703.522.0594
chunt@nafcu.org

National Association of Federal Credit Unions | www.nafcu.org

Carrie R. Hunt
Senior Vice President of Government Affairs
and General Counsel

April 4, 2014

The Honorable Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing and Trade
House Energy and Commerce Committee
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Jan Schakowsky
Ranking Member
Subcommittee on Commerce,
Manufacturing and Trade
House Energy and Commerce Committee
U.S. House of Representatives
Washington, D.C. 20515

Re: "Trolling for a Solution: Ending Abusive Patent Demand Letters"

Dear Chairman Terry and Ranking Member Schakowsky:

On behalf of the National Association of Federal Credit Unions (NAFCU), the only trade association exclusively representing the interests of our nation's credit unions, I write today in advance of next week's subcommittee hearing, "Trolling for a Solution: Ending Abusive Patent Demand Letters." On behalf of NAFCU member credit unions and the 97 million credit union members across the country, we appreciate the subcommittee's attention to this matter.

A growing number of credit unions are reporting receipt of demand letters from law firms representing patent assertion entities, claiming patent infringement, with the option to settle or face litigation. These deceptive letters are confusing and misleading as they often allege that the use of everyday technology violates the patent holders' rights. Further, these letters typically state vague or hypothetical theories of infringement, and often overstate or misinterpret the patent in question. Because the cost of litigation is often more expensive than paying a settlement amount, these "patent trolls" use the threat of litigation as leverage to extract payment from the recipient business who settles in lieu of running the risk of a complex and lengthy legal battle.

NAFCU believes a legislative solution is necessary to alter the intimidating business model used by these patent assertion entities and will continue to be supportive of any Congressional efforts to curb these practices.

Again, thank you for holding this important hearing today. If my staff or I can be of assistance to you, or if you have any questions regarding the impact of patent trolls on credit unions, please feel free to contact myself, or NAFCU's Director of Legislative Affairs, Jillian Pevo, at 703-842-2836.

Sincerely,

Carrie Hunt
Senior Vice President of Government Affairs & General Counsel

cc: Members of the Energy and Commerce Subcommittee on Commerce, Manufacturing, and Trade



Statement of the
National Retail Federation
National Council of Chain Restaurants
and
Shop.org
submitted to the
United States House
Energy and Commerce Subcommittee on Commerce, Manufacturing and Trade
for its hearing on
"Trolling for a Solution: Ending Abusive Patent Demand Letters"
held on
Tuesday, April 8, 2014

David French
Senior Vice President,
Government Relations

On behalf of:

National Retail Federation
1101 New York Avenue, Northwest
Suite 1200
Washington, D.C. 20005
(202) 783-7971
www.nrf.com

NATIONAL RETAIL FEDERATION
1101 New York Avenue, NW, Suite 1200
Washington, DC 20005
www.nrf.com

Chairman Terry, Ranking Member Schakowsky, and members of the House Energy and Commerce Subcommittee on Commerce, Manufacturing and Trade, on behalf of the National Retail Federation (NRF) and its divisions the National Council of Chain Restaurants and Shop.org, I appreciate the opportunity to submit this written statement to the Committee in connection with its hearing entitled "Trolling for a Solution: Ending Abusive Patent Demand Letters" held on April 8, 2014.

As the world's largest retail trade association and the voice of retail worldwide, NRF represents retailers of all types and sizes, including chain restaurants and industry partners, from the United States and more than 45 countries abroad. Retailers operate more than 3.6 million U.S. establishments that support one in four U.S. jobs – 42 million working Americans. Founded in 1996, Shop.org's 600 members include the 10 largest online retailers in the U.S. and more than 60 percent of the *Internet Retailer* Top 100 E-Retailers. The National Council of Chain Restaurants has worked to advance sound public policy that serves restaurant businesses and the millions of people they employ for over 40 years. NCCR members include the country's most respected quick-service and table-service chain restaurants. Shop.org is the world's leading community for digital retail, offering thought leadership through original research and gold-standard events and members include some of the world's largest and most respected retail, technology, research, and consulting companies. Contributing \$2.5 trillion to annual GDP, retail is a daily barometer for the nation's economy. Retailers create opportunities for life-long careers, strengthen communities at home and abroad, and play a leading role in driving innovation.

NRF appreciates continued congressional attention to patent troll abuse. Patent trolls are increasingly targeting traditional brick-and-mortar merchants, e-commerce companies, and chain restaurants alike. Trolls target retailers because, as end users of technology, they are more numerous than manufacturers and suppliers, and therefore are more profitable to the trolls. Trolls also know that retailers have less technological expertise to defend the allegedly infringing products. Retailers also operate on thin profit margins and do not have the resources to fight back.

Patent troll demands hamper technological innovation and adoption, crowd our court system, inhibit job creation, and ultimately drive up costs for retailers and prices for consumers.

At their core, demand letters use the threat of litigation as leverage to extract a "licensing fee" from the recipient business. Retailers often simply settle these nuisance claims rather than run the risk of protracted litigation in federal court. Put simply, it is often much more expensive to hire a lawyer to review or defend against a suspect claim than it is to pay the requested "fee." This is the trolls' business model.

No one knows just how many thousands of patent-related demand letters are sent out by trolls each year; statistics only track actual patent infringement litigation in federal courts. The troll has to actually file a case in court before a judge is even made aware of the infringement claim, therefore it is impossible to get an accurate understanding of the full breadth of this problem. We do know, however, that more and more retailers and chain restaurants have notified NRF of this escalating problem.

Retailers rarely take these cases to trial because the damages claims are so exorbitant, and the prospect of relief through litigation so time-consuming, that retailers make a business decision to settle, rather than litigate. It has been reported that trolls lose 92 percent of cases that do go to trial, but it is infrequent that a defendant has the fortitude to litigate.

End-user businesses such as retailers also appear to be easy prey because they often lack the legal resources and expertise to fight complex patent infringement claims. Many retailers do not even employ legal counsel in-house, let alone a highly specialized patent attorney. Ninety-one percent of retail companies operate with fewer than 20 employees and 95% of retail companies operate just one location.¹ Further, most retailers also do not have the time or money to engage in a lengthy battle with patent trolls. The average cost of fighting a patent troll is around \$2 million and takes about 18 months.² Patent trolls knowingly exploit their targets' tactical disadvantages, often pricing a settlement demand (which may still be in the millions) just below the cost of litigation, effectively blackmailing a retailer into settlement. This is an abuse of the system.

Trolls employ many pre-litigation tactics, including sending vague patent infringement letters demanding a licensing fee with no intention to ever file suit. Retailers typically receive short, two paragraph letters from a law firm demanding licensing settlements for use of a technology, process, or system.

To be clear, the technology at issue in many demand letters is ubiquitous technology. Virtually every retailer uses technology to conduct business in today's marketplace, and the trolls do not specifically state their claims, making it extremely difficult to discern what may be infringing.

Consulting a patent lawyer to determine the validity of the infringement claim and evaluate the license demand could cost tens of thousands of dollars. Moreover, the cost of litigating the claim in court or going to the Patent Trademark Office to challenge the patent could be prohibitive or imprudent to retailers, who operate on thin profit margins.

Retailers often settle these nuisance claims because it is much more expensive to consult with an attorney to determine the merits of the claim than it is to settle. Knowing this, trolls prey on retailers and send these deceptive letters en masse. It is important to the retail community that legislation adequately addresses the misleading correspondence trolls use.

Trolls' claims not only affect e-commerce applications and the everyday use of technology, but also affect the storefront operations of traditional "brick and mortar" retailers. Some real world examples of the latter are claims that purport to cover point of sale and inventory control equipment, including; scanning barcodes, printing receipts, the sale of gift cards, and the connection of any product, such as a computer or printer, to an Ethernet network.

The growing number of patent troll demand letters targets more practical applications as well. Recently, one troll filed suit against over a dozen retailers on a business method patent for

¹ 2007 Economic Census, thisisretail.org.

² Mark Gibbs, "A Patent Troll Wants to Charge You for Emailing Your Scans," *Forbes.com*, January 5, 2013.

conducting business over the Internet. E-commerce represented \$70 billion in the second quarter of 2013³ and claims of this nature threaten the future of the retail industry.

In some instances, it does not appear the law firms conduct any due diligence to truly ascertain whether a retailer is infringing its client's patent. Rather, based on conversations with many retailers, it appears that firms often simply pick the 150 biggest retailers in metropolitan areas and send the same vague demand letter to each of them.

Patent troll demand letters put the fear in retailers that a costly lawsuit could be forthcoming. Most retailers do not have patent litigators on staff or even on retainer. So, retailers can either ignore the letter at their own peril (and hope the harassment goes away) or begrudgingly try to settle for as little money as possible. In every case, settling is cheaper than litigating.

In some cases, retailers have incurred the expense of consulting a patent lawyer about demand letters and discovered that they do not even use the technology in question. When they inform the PAE that they use a different technology, PAEs still demand a settlement, just at a lesser amount.

Today, too many retailers and other Main Street businesses are diverting precious capital resources to settle with or fight patent trolls. This is capital that they could otherwise use to invest in their businesses and in their communities, including: creating jobs, fostering innovation, and maintaining their stores. Because the retail industry contributes \$2.5 trillion to our nation's annual GDP, loosening the grip of patent trolls on retailers and others will allow innovation and growth to flourish, and undoubtedly benefit the overall U.S. economy.

Patent trolls have taken advantage of brick and mortar stores, e-commerce sites, and chain restaurants by exploiting their inexperience in the traditional patent community through vague and broad demand letters. We are encouraged that Members of the Energy and Commerce Subcommittee on Commerce, Manufacturing and Trade recognize this abuse on main street businesses and the negative impact it has on our economy.

NRF members support legislative proposals to direct the Federal Trade Commission ("FTC") look into these unfair or deceptive demand letters and, using their current consumer protection enforcement powers, rein in bad actors that target Main Street businesses. Patent trolls should not have free reign to assert expired patents, make repeated and false threats of litigation to extort fees, and materially mislead the recipients of these demands. At the very least, patent trolls should be required to provide more details in their letters. Currently, the letters are effective because they lack specificity. Requiring more complete truthful disclosure will provide greater certainty to businesses, saving them time and money as they investigate the person or entity asserting the patent and determine the overall merits of the infringement claim.

Combating the rise of patent trolls is a top priority for retailers and chain restaurants. We look forward to discussing meaningful legislative solutions surrounding demand letter relief. We appreciate the Subcommittee's attention to this issue, and look forward to continuing our work together.

³ <http://research.nrffoundation.com/Default.aspx?pg=46#Um2vZuzD-00>

FRED UPTON, MICHIGAN
CHAIRMAN

HENRY A. WAXMAN, CALIFORNIA
RANKING MEMBER

ONE HUNDRED THIRTEENTH CONGRESS
Congress of the United States
House of Representatives
COMMITTEE ON ENERGY AND COMMERCE
2125 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6115
Majority (202) 225-2927
Minority (202) 225-3641

June 5, 2014

The Honorable William H. Sorrell
Attorney General
State of Vermont
109 State Street
Montpelier, VT 05609-1001

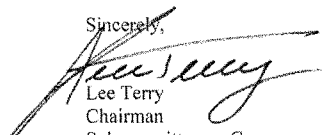
Dear Attorney General Sorrell,

Thank you for appearing before the Subcommittee on Commerce, Manufacturing, and Trade on Tuesday, April 8, 2014 to testify at the hearing entitled "Trolling for a Solution: Ending Abusive Patent Demand Letters."

Pursuant to the Rules of the Committee on Energy and Commerce, the hearing record remains open for ten business days to permit Members to submit additional questions for the record, which are attached. The format of your responses to these questions should be as follows: (1) the name of the Member whose question you are addressing, (2) the complete text of the question you are addressing in bold, and (3) your answer to that question in plain text.

To facilitate the printing of the hearing record, please respond to these questions by the close of business on Thursday, June 19, 2014. Your responses should be e-mailed to the Legislative Clerk in Word format at Kirby.Howard@mail.house.gov and mailed to Kirby Howard, Legislative Clerk, Committee on Energy and Commerce, 2125 Rayburn House Office Building, Washington, D.C. 20515.

Thank you again for your time and effort preparing and delivering testimony before the Subcommittee.

Sincerely,

Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing, and Trade

cc: Jan Schakowsky, Ranking Member, Subcommittee on Commerce, Manufacturing, and Trade
Attachment

Answers of Vermont Attorney General William H. Sorrell to Additional Questions of the Subcommittee on Commerce, Manufacturing, and Trade relating to the hearing entitled “Trolling for a Solution: Ending Abusive Patent Demand Letters” (testimony heard Tuesday, April 8, 2014).

The Honorable Lee Terry

1. In your experience with patent demand letters, how many contain fraudulent claims versus how many fail to provide adequate transparency on the patent or purported infringement, or both?

Both inadequate information and misleading information are serious problems. That is especially true for consumers/end users who are targeted with demand letters. Often it is a combination of extremely limited information and the misleading nature of the information provided that is particularly harmful.

For example, we have reviewed letters stating that the patent holder has identified the recipient as “likely” or “believed” to be infringing certain patents with little or no explanation of how this infringement is occurring. These letters are often sent indiscriminately without the patent holder having a reason to believe that there is infringement or that infringement is likely, making the claim regarding identifying the recipient misleading. This is coupled with limited or no information that would explain to the recipient exactly what they are doing to infringe the patents, making it difficult to formulate an adequate response to the letter. It is the combination of the misleading information and the omission of other information that makes it extraordinarily difficult for recipients to address the accusations and evaluate whether to license the patents or risk litigation.

2. What were the factors that you considered in formulating what elements indicated a bad faith demand letter?

As a state attorney general, I bring a consumer-protection focus to this issue. So a key question is whether a demand letter is deceptive or misleading to the average recipient; for example, a statement in a letter that threatens litigation within a specified period of time when the sender is not prepared or intending to file a lawsuit. That is the same standard we apply to commercial actors across the board. Other factors that may indicate bad faith include mass mailings of demand letters (which indicates a lack of investigation), demands for a response within an unreasonably short period of time, and lack of transparency.

Vermont passed legislation in 2013, which identified a number of factors that a court can consider in evaluating whether a person had made a bad faith assertion of patent infringement. Those factors include:

- (1) The demand letter does not contain the following information:
 - a. the patent number;
 - b. the name and address of the patent owner or owners and assignee or assignees, if any; and
 - c. factual allegations concerning the specific areas in which the target’s products, services, and technology infringe the patent or are covered by the claims in the patent.

- (2) Prior to sending the demand letter, the person fails to conduct an analysis comparing the claims in the patent to the target's products, services, and technology, or such an analysis was done but does not identify specific areas in which the products, services, and technology are covered by the claims in the patent.
- (3) The demand letter lacks the information described in subdivision (1) of this subsection, the target requests the information, and the person fails to provide the information within a reasonable period of time.
- (4) The demand letter demands payment of a license fee or response within an unreasonably short period of time.
- (5) The person offers to license the patent for an amount that is not based on a reasonable estimate of the value of the license.
- (6) The claim or assertion of patent infringement is meritless, and the person knew, or should have known, that the claim or assertion is meritless.
- (7) The claim or assertion of patent infringement is deceptive.
- (8) The person or its subsidiaries or affiliates have previously filed or threatened to file one or more lawsuits based on the same or similar claim of patent infringement and:
 - a. those threats or lawsuits lacked the information described in subdivision (1) of this subsection; or
 - b. the person attempted to enforce the claim of patent infringement in litigation and a court found the claim to be meritless.

9 V.S.A. § 4197

The Honorable Jan Schakowsky

1. **Some state and federal legislative proposals to address abusive patent demand letters include provisions specifying exactly what information such letters must include. A list of commonly suggested requirements is below. Please provide the Subcommittee with your written views on whether patent demand letters should include:**

- a. **Description of each patent being infringed, including patent number;**

Yes. At a minimum the recipient of a patent demand letter needs the patent number to understand how its actions could be infringing a patent. A brief description of the patent will allow a lay person, without expertise in the field of the patent, a general understanding of the scope of the patent. The patent number will allow the recipient to conduct further research on the history, claims, and validity of the patent.

- b. **Description of each claim of the patent being infringed;**

Yes. Patents can contain a significant number of claims. Infringement of a single claim constitutes infringement of the patent. By requiring disclosure of the claims that are allegedly being infringed, a recipient has a better chance of actually evaluating whether its actions are infringing.

- c. **Description of the infringing device, method, or service;**

Yes. Directing an alleged infringer to the device, method, or service that is allegedly infringing the patent is necessary for the recipient of the letter to evaluate whether the device, method, or

service is, in fact, infringing. Receiving a letter threatening infringement and identifying the patents, without further information about what is infringing, leaves the recipient, again, with inadequate information

d. Description of how the device, method, or service infringes;

Yes. This is necessary to place on the patent holder the burden of connecting the allegedly infringing activity to the patent. Without a description of how the device, method, or service infringes, it is necessary for the recipient of a letter to take the patent and the device, method, or service to an attorney or expert in the area for analysis before it is clear whether the patent holder has even attempted to do this analysis. This is an unreasonable cost to impose on small businesses and non-profits that receive these letters. The letters should not be sent until the patent holder is able to provide such a description.

e. Identification of the owner of the patent;

Yes. Knowing the owner of the patent allows the recipient of a demand letter to better research previous lawsuits with respect to the patent or patent family, previous settlements, and previous licensing campaigns. This information, which is not burdensome, and is necessary if the recipient decides to affirmatively challenge the patents.¹

f. Identification of the parent company, if any, of the patent owner;

Yes. This is valuable for the same reason that knowing the owner is valuable. In many circumstances, the nominal owner is a shell corporation. Identifying the parent company will help recipients understand the true party with a financial interest in the assertions made in the demand letter.

g. Identification of the parent company, if any, of the sender of the letter;

Yes. In some circumstances the sender of the letter may not be the patent owner but may, in some way, be related to the patent owner. For example, we have seen a campaign where the same patent was enforced through over eighty subsidiaries of the patent owner. These subsidiaries were not the patent owner, but rather claimed an exclusive license to enforce the patents. Identifying the parent company of the sender would have allowed recipients to more easily connect with others who had received similar letters.

h. Address of the patent owner and, if a business, also the place of incorporation, principal place of business, and principal business address within the recipient's state;

Yes. This basic information allows the recipient of the letter to contact the patent owner with respect to inquiries regarding the patent and the demand letter.

i. Address of the sender of the letter and address of the parent company of the sender of the letter;

¹ Fed. R. Civ. P. 19(a)(1)(B); *Al23 Sys. v. Hydro-Quebec*, 626 F.3d 1213, 1217 (Fed. Cir. 2010) (“[A]n accused infringer must likewise join both the exclusive licensee and the patentee in a declaratory action because the patentee is a necessary party.”).

Yes. This provides an alternative contact for the recipient of the letter. It may be an attorney of the patent owner or an exclusive licensee of the patent. It again allows an open line of communication to resolve any potential dispute in advance of litigation.

j. Contact information for a person who can discuss resolution;

Yes. If there is a legitimate dispute, the recipient should be readily able to reach a person authorized to discuss potential resolutions to any patent infringement.

k. Identification of persons other than the patent owner who may benefit from enforcement;

Yes. The party who will financially benefit from a negotiated agreement may be shielded through layers of shell corporations. This information is, however, important and material to the recipient and may influence the recipient's course of action. For instance, the letter recipient may have an existing business relationship with that party. Knowing this information may allow the parties to more efficiently address the allegations in the letter.

l. Identification of any person with the right to enforce each patent;

Yes. This is necessary to assure that all appropriate persons are parties to any agreement that may be reached.

m. Identification of all persons that have been granted a license to the patent;

Yes. This information should be made available, for example by providing a link to a website. It is common for patent demand letters to state or imply that other similarly situated individuals or businesses have purchased licenses. This information would allow the recipient to identify, and if appropriate, speak with others who have purchased a license. It will cut down on deceptive assertions about other licenses.

n. Notice to the recipient that he or she may have the right to have the manufacturer defend the case; and

Yes. End-users of off-the-shelf technology are often surprised and confused when they receive patent demand letters. They did not develop the technology, and they are simply using it for its intended purpose. They often lack the expertise to evaluate whether their actions are, in fact, infringing the asserted patents. Notification that the manufacturer may defend the case helps provide this end-user with guidance with respect to appropriate next steps. It allows them to evaluate their options with full knowledge of the potential resources that may be available.

o. Some factual basis for the licensing fee or settlement amount demanded.

Yes. The patent holder or sender of a patent enforcement letter and the recipient of such a letter are not on an even playing field. The information disconnect is extraordinary. The patent holder sets a licensing fee as an alternative to costly litigation. The licensing fee is commonly less than the cost of litigation or even hiring an attorney to evaluate the patents, making it appealing to the recipient. The patent owner knows who has received previous letters, the response to previous

letters, the typical price for a license, and why the price was set where it was. With many of these letters, it is not a sophisticated negotiation between equals. Instead, it is a negotiation between a patent holder with full knowledge of the value of the patents, previous licensing arrangements, and the success of the campaign and the recipient who has almost no information regarding the validity, scope, or value of the patents and faces high cost litigation risk if a license is not purchased. In this instance, basic factual information regarding the basis for the offered licensing fee or settlement is a very small step in creating transparent negotiations.

The Honorable Peter Welch

1. At the Subcommittee hearing on April 8, 2014, I asked the following question, but there was no time remaining for a response. Therefore, please answer in writing: what evidence do we have about the effect of patent trolls on suppressing innovation?

My office looks at this issue primarily from the perspective of consumer protection. Patent trolls often intimidate small businesses and nonprofits that use off-the-shelf technologies. In these types of campaigns, the patent trolls are not necessarily suppressing innovation, but they are limiting or interfering with entrepreneurs and deferring resources that could otherwise be spent helping these businesses expand and better serve their customers. According to published accounts, tech businesses in Vermont have been harmed by patent trolling. One Vermont business, MyWebGrocer, an Internet software company, has reported costs of over \$100,000 over the last four years to address patent trolls. Additionally, MyWebGrocer had a multimillion-dollar project, which would have resulted in the hiring of new employees, interrupted because potential customers received patent demand letters that they were forced to address.² Patent trolling has real costs for the Vermont economy.³

Although suppression of innovation within the technology industry is not an issue my office has particularly focused on, it is also a real concern. Technology companies face the largest number of lawsuits from patent assertion entities.⁴ Microsoft has testified that it typically has sixty pending infringement claims from patent assertion entities, costing tens of millions of dollars.⁵ Similarly, Google, Blackberry, Earthlink, and Red Hat have also seen significant increases in litigation defense costs.⁶ In addition to costing large innovators significant amounts of money, which can then not be used for innovation, small innovators may also be harmed. A recent study has concluded that venture capital investment would have likely been \$21.772 billion higher over

² See John Herrick, *Vermont Businesses Want to See Patent Troll Legislation Go National*, vtdigger.org, Sep. 30, 2013, <http://vtdigger.org/2013/09/30/vermont-businesses-want-see-patent-troll-legislation-go-national/>

³ 9 V.S.A. § 4195(a)

⁴ 2013 NPE Litigation Report 26, RPX Corporation (2013) (Listing defendants of non-practicing entity lawsuits by sector: 28% - E-commerce and Software; 12% - Consumer Electronics and PCs; 10% - Networking; 10% - Mobile Communications and Devices).

⁵ Phil Goldberg, *Stumping Patent Trolls on the Bridge to Innovation*, Progressive Policy Institute, 6 (Oct. 2013).

⁶ *Id.*

the last five years without the litigation brought by “frequent litigators.”⁷ In addition to the high costs of litigation diverting resources, aggressive enforcement of questionable patents can lead to companies forgoing research and development in certain fields.⁸

The Honorable Bobby Rush

1. **At the Subcommittee hearing on April 8, 2014, we heard testimony asking that federal legislation preempt state laws regarding enforcement letters. Could you please discuss how this would impact consumers?**

Preemption of state enforcement authority would harm consumers. If federal legislation preempts state laws, it limits the ability of states to flexibly and efficiently react to changes in practices and behaviors that are not addressed by the federal legislation. While federal legislation may address the problems that currently exist with respect to unfair and deceptive patent demand letters, bad actors will surely find ways to circumvent the requirements and continue to engage in unfair and deceptive acts. By preempting state law, the federal government would tie the states’ hands in addressing those changes. States are already limited in the scope of authority that they have in this area. Many of the concerns that stakeholders express with the patent system – vague patents, high litigation costs, etc. – are beyond the purview of state laws. States do, however, have authority to protect consumers from unfair and deceptive acts and practices in commerce. Preempting state laws further will eliminate the already limited tools that states have to protect businesses and individuals against bad actors.

Consumer protection is a core state police power. It is unusual for Congress to preempt state authority in this area. While states are typically guided in enforcement of their consumer protection acts by the FTC Act,⁹ the Act does not typically preempt state authority to enforce their own statutes.¹⁰ It is common for federal consumer protection statutes to operate concurrently with state authority.¹¹ The proposed legislation should not limit the states’ ability to protect their residents from unfair or deceptive conduct.

⁷ Catherine E. Tucker, *The Effect of Patent Litigation and Patent Assertion Entities on Entrepreneurial Activity* 36 (May 15, 2014) (using frequent litigators as a proxy for patent litigation brought by patent assertion entities), available at <http://cdn.arstechnica.net/wp-content/uploads/2014/06/Tucker-Report-5.16.14.pdf>.

⁸ *To Promote Innovation: The Proper Balance of Competition and Patent Law Policy*, Federal Trade Commission Ch. 3, 36-37 (2003) (explaining that “patent thickets” in the area of computer hardware harm innovation by requiring companies to expend extensive resources on patent portfolios and defense, reducing follow-on innovation, and causing uncertainty).

⁹ See, e.g., 9 V.S.A. § 2453(b); see also Henry N. Butler, *Are State Consumer Protection Acts Really Little-FTC Acts?* 10 (Northwestern University School of Law Scholarly Commons, Faculty Working Papers, 2010) (“Twenty-eight states currently reference the FTC in their CPA.”).

¹⁰ See *Altria Group, Inc. v. Good*, 555 U.S. 70, 91 (2008) (concluding that FTC decisions did not prevent a jury from considering a state deceptive practices claim).

¹¹ See, e.g., Telephone Consumer Protection Act, 47 U.S.C. § 227(g)(6) (“Nothing contained in this subsection shall be construed to prohibit an authorized State official from proceeding in State court on the basis of an alleged violation of any general civil or criminal statute of such State.”); Real Estate Settlement Procedures Act, 12 U.S.C. § 2616 (“This chapter does not annul, alter, or affect, or exempt any person subject to the provisions of this chapter from complying with, the laws of any State with respect to

settlement practices, except to the extent that those laws are inconsistent with any provision of this chapter, and then only to the extent of the inconsistency.”); Truth in Lending Act, *Williams v. First Gov’t Mortgage & Investors Corp.*, 176 F.3d 497, 500 (D.C. Cir. 1999) (finding that TILA did not preempt the District of Columbia Consumer Protection Act “and that TILA compliance does not immunize lenders . . . against CPPA [D.C. Consumer Protection Procedures Act] liability.”); Telemarketing and Consumer Fraud and Abuse Prevention Act, 15 U.S.C. § 6103(f)(1) (“Nothing contained in this section shall prohibit an authorized State official from proceeding in State court on the basis of an alleged violation of any civil or criminal statute of such state.”); Fair Debt Collection Practices Act, 15 U.S.C. § 1692n (“This subchapter does not annul, alter, or affect, or exempt any person subject to the provisions of this subchapter from complying with the laws of any State with respect to debt collection practices, except to the extent that those laws are inconsistent with any provision of this subchapter, and then only to the extent of the inconsistency. For purposes of this section, a State law is not inconsistent with this subchapter if the protection such law affords any consumer is greater than the protection provided by this subchapter.”).

FRED UPTON, MICHIGAN
CHAIRMAN

HENRY A. WAXMAN, CALIFORNIA
RANKING MEMBER

ONE HUNDRED THIRTEENTH CONGRESS
Congress of the United States
House of Representatives
COMMITTEE ON ENERGY AND COMMERCE
2125 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6115
Majority (202) 225-2927
Minority (202) 225-3641

June 5, 2014

Mr. Rheo Brouillard
President and CEO
Savings Institute Bank and Trust Company
803 Main Street
Willimantic, CT 06226

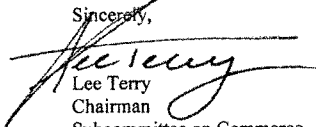
Dear Mr. Brouillard,

Thank you for appearing before the Subcommittee on Commerce, Manufacturing, and Trade on Tuesday, April 8, 2014 to testify at the hearing entitled "Trolling for a Solution: Ending Abusive Patent Demand Letters."

Pursuant to the Rules of the Committee on Energy and Commerce, the hearing record remains open for ten business days to permit Members to submit additional questions for the record, which are attached. The format of your responses to these questions should be as follows: (1) the name of the Member whose question you are addressing, (2) the complete text of the question you are addressing in bold, and (3) your answer to that question in plain text.

To facilitate the printing of the hearing record, please respond to these questions by the close of business on Thursday, June 19, 2014. Your responses should be e-mailed to the Legislative Clerk in Word format at Kirby.Howard@mail.house.gov and mailed to Kirby Howard, Legislative Clerk, Committee on Energy and Commerce, 2125 Rayburn House Office Building, Washington, D.C. 20515.

Thank you again for your time and effort preparing and delivering testimony before the Subcommittee.

Sincerely,

Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing, and Trade

cc: Jan Schakowsky, Ranking Member, Subcommittee on Commerce, Manufacturing, and Trade
Attachment

Additional Questions for the RecordThe Honorable Lee Terry

1. **You testified that you found out the cases filed by ATL against other banks were dismissed and not settled. How did you discover this?**

I have been working with and following the progress being made by Attorney Robert Stier of the firm Pierce Atwood LLP of Portland Maine, who has been following the case before Judge Robinson in the Delaware courts. The case was brought by Automated Transactions (ATL – the patent troll) against the parent of the 7-Eleven convenience store chain. The firm refused to settle and has since been defending itself against ATL's claims. Judge Robinson ruled in favor of 7-Eleven, noting that the primary patent and several related patents were invalid. ATL appealed the ruling and earlier in 2014 the Supreme Court refused to hear ATL's appeal.

Attorney Stier, on behalf of a number of banks, including Savings Institute Bank & Trust, filed several motions, one consolidating the cases from the various states to the same Delaware court and also a "Rule 11 motion", for sanctions against ATL, asserting that it brought baseless claims against banks even after being advised that these banks are not subject to the patent assertions and even after the Court invalidated several of the patents continuing to be asserted.

You testified that even when a company knows there is no legal standing to a patent demand, fighting the demand costs more than settling the matter for a license fee. Are there alternatives to going to court?

I am not aware of any alternatives other than settling or going to court.

The Honorable Jan Schakowsky

1. **Some state and federal legislative proposals to address abusive patent demand letters include provisions specifying exactly what information such letters must include. A list of commonly suggested requirements is below. Please provide the Subcommittee with your written views on whether patent demand letters should include:**
 - a. Description of each patent being infringed, including patent number;
 - b. Description of each claim of the patent being infringed;
 - c. Description of the infringing device, method, or service;
 - d. Description of how the device, method, or service infringes;
 - e. Identification of the owner of the patent;
 - f. Identification of the parent company, if any, of the patent owner;
 - g. Identification of the parent company, if any, of the sender of the letter;
 - h. Address of the patent owner and, if a business, also the place of incorporation, principal place of business, and principal business address within the recipient's state;
 - i. Address of the sender of the letter and address of the parent company of the sender of the letter;
 - j. Contact information for a person who can discuss resolution;
 - k. Identification of persons other than the patent owner who may benefit from

enforcement;

- l. Identification of any person with the right to enforce each patent;**
- m. Identification of all persons that have been granted a license to the patent;**
- n. Notice to the recipient that he or she may have the right to have the manufacturer defend the case; and**
- o. Some factual basis for the licensing fee or settlement amount demanded.**

I believe most, if not all, of this information should be required. As a user of a service provided by a third party vendor I, and businesses like mine, are in no position to know what patents may be applicable for parts used within the equipment we employ. Certainly the letter we received from the "troll" which simply listed a series of numbers and provided a two week window in which to "settle" is insufficient. I would therefore add to the above list 1) that a reasonable response time be included and 2) the results of any investigation done by the patent holder substantiating their claim that their patent has been infringed.

The Honorable Peter Welch

- 1. At the Subcommittee hearing on April 8, 2014, I asked the following question, but there was no time remaining for a response. Therefore, please answer in writing: what evidence do we have about the effect of patent trolls on suppressing innovation?**

Patent trolls harm the overall economy by forcing small companies and non-profits to divert resources from more productive use. Rather than having capital to hire more staff and serve more consumers businesses attacked by trolls are forced to make significant settlement arrangements or retain counsel to defend themselves against frivolous claims. In my opinion, smaller companies which are the engine of innovation and job creation in this country are being stifled by patent trolls.

FRED UPTON, MICHIGAN
CHAIRMAN

HENRY A. WAXMAN, CALIFORNIA
RANKING MEMBER

ONE HUNDRED THIRTEENTH CONGRESS
Congress of the United States
House of Representatives
COMMITTEE ON ENERGY AND COMMERCE
2125 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6115
Majority (202) 225-2927
Minority (202) 225-3641

June 5, 2014

Mr. Dennis C. Skarvan
Deputy General Counsel
Intellectual Property
Caterpillar Incorporated
100 N.E. Adams Street
Peoria, IL 61629

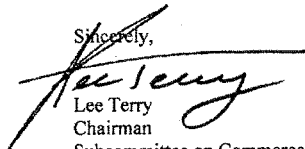
Dear Mr. Skarvan,

Thank you for appearing before the Subcommittee on Commerce, Manufacturing, and Trade on Tuesday, April 8, 2014 to testify at the hearing entitled "Trolling for a Solution: Ending Abusive Patent Demand Letters."

Pursuant to the Rules of the Committee on Energy and Commerce, the hearing record remains open for ten business days to permit Members to submit additional questions for the record, which are attached. The format of your responses to these questions should be as follows: (1) the name of the Member whose question you are addressing, (2) the complete text of the question you are addressing in bold, and (3) your answer to that question in plain text.

To facilitate the printing of the hearing record, please respond to these questions by the close of business on Thursday, June 19, 2014. Your responses should be e-mailed to the Legislative Clerk in Word format at Kirby.Howard@mail.house.gov and mailed to Kirby Howard, Legislative Clerk, Committee on Energy and Commerce, 2125 Rayburn House Office Building, Washington, D.C. 20515.

Thank you again for your time and effort preparing and delivering testimony before the Subcommittee.

Sincerely,

Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing, and Trade

cc: Jan Schakowsky, Ranking Member, Subcommittee on Commerce, Manufacturing, and Trade
Attachment

Additional Questions for the Record – Dennis Skarvan, 21CThe Honorable Lee Terry

1. You warned against sweeping in business-to-business communications and inadvertently chilling legitimate patent communications.

- a. Can you provide examples of such communications?

Answer: The patent laws already contain provisions that encourage disclosure of the existence, ownership and identity of relevant patents. The ability to freely communicate concerning one's patent rights is important to complying with these provisions, as well as to furthering day-to-day business transactions.

As to ownership, 35 U.S.C. 261 specifies that "patents shall have the attributes of personal property." It further specifies that a patent, or any interest therein, shall be assignable in law by an instrument in writing, and that assigns or legal representative may in like manner grant and convey an exclusive right for the whole or any specified part thereof in the United States. If certified as specified in this section, an assignment, grant or conveyance of a patent or patent application shall constitute prima facie evidence of such transfer. Most importantly, 35 U.S.C. 261 specifies that any assignment, grant or conveyance "shall be void as against any subsequent purchaser or mortgagee for valuable consideration, without notice, unless it is recorded in the Patent and Trademark Office within three months from the date or prior to the date of such subsequent purchase or mortgage." Accordingly, Section 261 imposes an obligation of notice and/or timely recording of conveyances of interests in patents, placing patent owners at jeopardy that their assignments will be void against subsequent purchasers in certain circumstances in the absence of notice.

*As to articles covered by a patent, 35 U.S.C. 287 places an obligation upon patentees, and persons making, offering for sale, or selling such articles within the United States to provide notice to the public of the patent by marking the product with its patent number(s), or by providing actual notice to the infringer. Although patentees invariably endeavor to ensure articles covered by their patents are marked, especially when licensees are involved, issues arise as to whether lapses in marking have occurred that might serve to deny recoveries for pre-suit infringement. Because Section 287 further specifies that in the event the patented articles are not properly marked, "no damages shall be recovered by the patentee in any action for infringement, **except on proof that the infringer was notified of the infringement and continued to infringe thereafter**, in which event damages may be recovered only for infringement occurring after such notice." (bolding added), most patentees seek to avoid marking disputes by providing actual notice to infringers, as soon as their infringements are identified. Such early notice is also beneficial to the alleged infringer who may then alter its course of conduct, seek a license, or otherwise mitigate its potential exposure.*

Whether such notice was sufficient to be effective under this section is a matter to be decided by the trier of fact, although existing precedent generally requires that the notice come from

the patentee or his/her/their representative and that both the allegedly infringed patent and accused infringement be specifically identified. See "Prerequisites to Recovery of Damages: Importance of Marking and Notice of Infringement," Edward W. Remus & Heather Bjella, <http://www.mcandrews-ip.com/files/article/Remus-Bjella%20BNA%20Marking%20article%20-%202010%20update.pdf>. Under current law, a patentee's failure to provide effective notice leaves it at some jeopardy of failing to collect substantial damages.

Other provisions of the patent laws also require or encourage placing infringers on actual notice. In cases where the alleged infringement is by inducement under 35 USC 271(b), it is usually necessary to show that the alleged inducer had knowledge of the patent at issue, and knew or should have known that the infringement was being induced. Similarly, recoveries of damages under 35 U.S.C. 271(g) may be limited by operation of Section 287(b)(1), which requires that persons subject to liability for practicing a patented process have "knowledge before the infringement that a patented process was used to make the product the importation, use, offer for sale, or sale of which constitutes the infringement" and Section 287(b)(2) that the person subject to liability "had notice of infringement with respect to that product." As specified in subsection (b)(5)(A) of Section 287, "notice of infringement means actual knowledge, or receipt by a person of a written notification, or a combination thereof, of information sufficient to persuade a reasonable person that it is likely that a product was made by a process patented in the United States." Part (B) of this subsection specifies that a

"written notification from the patent holder charging a person with infringement shall specify the patented process alleged to have been used and the reasons for a good faith belief that such process was used. The patent holder shall include in the notification such information as is reasonably necessary to explain fairly the patent holder's belief, except that the patent holder is not required to disclose any trade secret information."

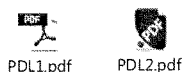
With respect to assertions of infringement under Section 271(g), potential infringers are further protected through "request for disclosure" process which allows third parties to make a request "to a person then engaged in the manufacture of a product to identify all process patents owned by or licensed to that person, as of the time of the request, that the person then reasonably believes could be asserted to be infringed under section 271(g) if that product were imported into, or sold, offered for sale, or used in, the United States by an unauthorized person." 35 U.S.C. 287(b)(4).

Effective actual notice of infringement is often also important to patentees who are seeking to prove that a defendant's conduct constituted willful infringement, such that attorney fees should be awarded pursuant to 35 U.S.C. 285.

In addition to the foregoing statutory requirements, patentees seeking to resolve infringement disputes without resorting to litigation already have strong incentives to communicate candidly with persons suspected of infringement, particularly once an agreement has been entered to preclude the premature filing of a declaratory judgment action and suitable terms of confidentiality have been reached. It is far more efficient for all involved to quickly arrive at a common understanding of the issues, and their potential pre-litigation settlement, than to force them into lengthy and expensive court proceedings.

The foregoing are but a few examples of the importance of not just allowing, but of encouraging, patent owners to freely communicate about their patents, and any actual or suspected infringements thereof.

Attached below are copies of actual business-to-business communication, redacted only to delete references to the parties involved. To open these files, right click on a file, select "Packager Shell Object Object," and then "Activate Contents."



It should be emphasized that the communications shown here are never sent to hundreds of individuals and small businesses.

- b. Can you give us examples of legislative language, either pending in the Senate or in the States, which you believe would do just that?

Answer: To our knowledge, state legislation, either passed or pending, in Vermont, Alabama, and Virginia are examples of legislation with overbroad provisions that would sweep-in business-to-business communications. Bills similar to the above have been passed or are pending in Idaho, Georgia, Maryland, Utah, South Dakota, Wisconsin, Oregon, Ohio, and Maine.

An example of state legislation that does not raise this concern passed and is pending executive action in Illinois. Louisiana has passed legislation which does not create a private cause of action.

2. It sounds reasonable to include things like the name of the person or entity that holds the rights to a patent, or to identify the infringed patent by number, but we've also heard concerns that this may not always be possible. Why would it not be possible to identify these two things at a minimum?

Answer: In many cases, the patent number and its owner can be identified; but there are valid reasons why this is not possible in every case. Federal Circuit law and substantive patent law has evolved to the point where business-to-business communications often require a general letter to an infringer or a potential licensee to open up discussions without identifying the patent owner or a patent number in order to avoid the infringer or licensee from filing a declaratory judgment action against the patent owner in a favorable venue for the infringer or licensee. Generally, a letter will be sent to initiate discussions with expectation that the parties will later reach an agreement that all discussions will be kept confidential and will not be a basis for a declaratory judgment action. Requiring the patent number and the name of the patentee would allow infringers or licensees to gain an advantage over the patent owner, potentially loading federal courts with additional, unnecessary, patent cases that should never have been filed. The key to whether sanctions should be provided, however, is whether information is provided in bad faith: situations where the sender makes knowingly false or knowingly misleading statements or

representations, or makes such statements or representations with conscious disregard of their false or misleading nature.

While the list of “commonly suggested requirements” set forth in this question may be desirable to include in some demand letters, it is not always possible and/or desirable to include such information in every demand letter. For example, often it may be appropriate to include the patent number, the owner of the patent and the parent company, if any, of the patent owner. On the other hand, some of the “commonly suggested requirements” in this question go beyond what is needed to put the recipient on fair notice of the nature or purpose of the communication and are unduly burdensome for patent owners. Such overly-burdensome requirements include, for example, a “description of each claim of the patent being infringed.” Often the information needed to identify each claim of the patent believed to be infringed is solely within the control of the recipient, and imposing such a requirement on the patent holder, at the risk of being charged with sending a bad-faith demand letter if it is not included, would be unfair to patent owners and would curtail legitimate patent licensing and enforcement communications.

Even for the “commonly suggested requirements” that may be appropriate in the case of some demand letters, they may not be appropriate for all letters. A list of the patent numbers the sender may believe are being infringed, for example, may not be appropriate to require in each demand letter. In the case of legitimate business-to-business letters, often an initial communication from the patent owner may be designed to offer a license to an entire patent portfolio, in which case the specific patent numbers may be provided in later communications once the parties have entered into a nondisclosure agreement. Indeed, under current patent law, the patent owner should not be required in all cases to include the patent number in an initial communication, because it may subject the patent owner to the risk that the recipient may file a declaratory judgment action against the patent owner in a venue unfavorable to the patent owner. As a result, the initial communication may invite the recipient to enter into a nondisclosure and standstill agreement, under which the parties may then exchange detailed information about the patents under consideration and the recipient’s products, processes or business interests. Requiring each demand letter to include a list of the patent numbers the sender may believe are being infringed would disrupt this process and impede these legitimate types of patent communications.

To be clear, bad-faith demand letters are a problem and we strongly support finding a fair and effective solution to end them. At the same time, however, legislation in this area must reflect the balance necessary to ensure that efforts to address patent demand letter abuses do not inadvertently chill the legitimate patent communications patent owners engage in each and every day. The patent system is designed to encourage notice and communication of patent rights as an efficient way to resolve infringement disputes short of filing lawsuits, as well as to promote the licensing and dissemination of new technologies.

There is a distinct and critically important difference between those who send false and misleading demand letters to small businesses, retailers and banks and the vast majority of patent holders, including individual inventors and universities, who legitimately send notices to alert the public of their patent portfolios, to offer them for license and, when necessary, to prevent their patented products from being infringed.

The key to legislation that appropriately recognizes this distinction and targets abusive demand letters, while not chilling legitimate patent licensing and enforcement communications, is to identify a basic set of information typically appropriate to be included in patent demand letters that fairly balances the recipient's need for information against the burden and risk to the patent owner of providing such information, and then to authorize enforcement authority to be brought against letters that do not contain such information only when the information is not provided in bad faith – i.e., in an effort to mislead or deceive the recipient. This approach protects legitimate patent communications and appropriately targets enforcement authority to those who need protection against bad-faith demand letters. The enforcement resources of the FTC and state Attorneys General are finite and should not be called upon to aid recipients of legitimate patent licensing communications, or companies that are fully capable of defending themselves against demand letters. It also ensures that the legislation is narrowly-tailored to mitigate First Amendment concerns associated with the regulation of demand letters, which courts have held are subject to the constitutional protections afforded to petitioning the government for redress.

In the following sections, we explain in more detail our views on the list of “commonly suggested requirements” for patent demand letters.

3. You raised First Amendment concerns regarding any “provisions seeking to mandate...[what patent owners] must say when communicat[ing] information[.]” Are there any disclosure requirements that would not be objectionable?

Answer: Yes. Disclosure requirements that would reveal that a communication was false or fraudulent would not be objectionable. Such communications are not protected by the First Amendment.

4. You testified that the “vast majority of patent owners send patent ‘enforcement’ letters.” What do patent “enforcement” letters look like compared to patent “demand” letters?

Answer: As shown in the examples provided in response to question 1a above, patent enforcement letters are generally business-to-business letters – letters not sent in “bad faith” – that inform the recipient that a patent issue exists between the companies and generally propose a way to resolve the issue. They do not contain false or misleading information about a patent issue or assert patents in a way that is false or fraudulent.

Demand letters have taken on a legislative meaning that they can contain false or misleading information about a patent issue or assert patents in a false or fraudulent manner. Such demand letters are also generally sent to many recipients (100 or more) in order to coerce a settlement that is a fraction of the costs of defending an action asserting a false or fraudulent claim of infringement.

5. You commented that “[m]any of the legislative proposals address written communication which states that the intended recipient or any person affiliated with the intended recipient is, or may be, infringing a patent.” You critiqued these measures as “contain[ing] no

meaningful limits to protect patent owners legitimately communicating their rights.” What kind of limits do you believe are necessary?

Answer: So as not to impede legitimate business to business communications, any legislation should clearly spell out those objectively-identifiable acts or practices that are deemed unfair or deceptive. This may include false statements of patent ownership or of the right to enforce or license patents, as well as the lack of basic information and specificity in the demand letter that would allow recipients to make informed decisions, leaving them vulnerable to abuse. But determinations of the merits or sufficiency of allegations of patent infringement included in demand letters are questions of substantive patent law, not consumer protection. The role of the legislation should be to protect the recipients of demand letters against false or materially misleading statements of fact, not to stray into substantive patent law by weighing in on the merits or sufficiency of patent disputes.

Examples of false or materially misleading communications include:

- (1) the communications falsely state that litigation has been filed against the recipient;
- (2) the communications falsely state that litigation for infringement of the patent has been filed against persons other than the recipient;
- (3) the person asserting the patent is not a person with the right, or does not represent a person with the right, to license or enforce the patent at the time the communication is sent;
- (4) the communications seek compensation for a patent claim that has been held to be invalid in a final determination;
- (5) the communications state the sender, a subsidiary of the sender, or an affiliate of the sender previously filed a civil action in which a claim for infringement of the patent against one or more defendants similarly situated to the recipient when the sender knew or should have known such claim was held to be invalid in a final determination;
- (6) the communications seek compensation for activities undertaken by the recipient after expiration of a patent asserted in the communications;
- (7) the communications falsely state that the sender is the exclusive licensee of any patent asserted in the communications;
- (8) the communications seek compensation for activity of the recipient that the sender knew or should have known were covered by a license relating to the patent asserted between the sender and the manufacturer of the product or service;
- (9) the communications falsely state persons similarly situated to the recipient purchased a license for a patent asserted in the communications;

(10) the communications state persons similarly situated to the recipient purchased a license and the sender knew or should have known such license is unrelated to the alleged infringement or the patent asserted in the communications; or

(11) the communications falsely state that an investigation of the recipient's alleged infringement occurred.

6. In a patent rights assertion letter, is it always possible to identify:

a. The patent being infringed?

Answer: The patent system is designed to encourage notice and communication of patent rights as an efficient way to resolve infringement disputes short of filing lawsuits, as well as to promote the licensing and dissemination of new technologies. Those activities comprise the vast majority of letters sent to notify the recipients of the existence of patent rights. There is a distinct and critically important difference between such "patent enforcement letters" and the bad faith patent demand letters containing false and misleading statements sent to hundreds of small businesses, retailers and banks. Unlike the few opportunistic patent assertion entities that send bad faith patent demand letters to extort settlements from innocent end users, the vast majority of patent holders, including individual inventors and universities, legitimately send notices to alert the public of their patent portfolios, to offer them for license and, when necessary, to prevent their patented products from being infringed. While it is desirable to identify the patent being infringed in a patent enforcement letter, there are reasons and situations where it would be appropriate, indeed, advisable to not include such information in a letter. In order to avoid an infringer or potential licensee from filing a declaratory judgment action, a patent owner may not want to identify a specific patent in an initial patent enforcement letter. Rather than demand a specific list of requirements for such letters to contain, it would be far better for legislation to focus on the question of whether a letter contains false and misleading information that would transform it into a bad faith demand letter that is designed to intimidate or coerce the recipients into extortionist settlements.

b. The activity or product that allegedly infringes on the asserted patent?

Answer: While it is desirable to identify the activity or product that infringes, it may be impossible for a patent owner to know the specific activity used in a method or process by an infringer since the infringer's manufacturing process is kept secret. Further, it is often impossible to separate chemical ingredients in a product or to determine the exact proportions used by an infringer in its secret formulations. Also, in some cases, the patent owner simply may not have access to the infringing product.

c. How the activity or product specifically infringes the asserted patent?

Answer. As noted above in 6b, it is often impossible to reverse engineer a product to learn the exact steps in a method or process of manufacture without specific knowledge of the infringer's formulations or methods. This often requires discovery from the

infringer in order to understand and know the details. This is why business-to-business patent enforcement letters may identify a product or a belief about a method used, but cannot with specificity identify the specific ingredients, parts, or subcombinations in a product or the specific steps of a process.

- d. Identify the patent owner?

Answer: While a patent owner can generally be identified and disclosed in a business-to-business patent enforcement letter (and must be disclosed in any litigation under the Federal Rules of Civil Procedure), the complexity of ownership of patents, and the free transferability of patents, often makes it difficult and expensive to identify all the owners or licensees of a patent, especially in today's complex corporate environments in which many, many subsidiaries are licensed under, or have a partial ownership interest in, a patent.

- e. Identify the letter writer's role?

Answer: Generally, yes. The letter writer and the role he or she plays can almost always be identified from the letterhead, salutation, or body of the letter. Letters are often written by outside counsel on their letterhead.

- f. Provide a point of contact?

Answer: Again, generally, yes. The address and name of the author of a letter will be present and provides a point of contact.

If the answer to any of these questions is no, please explain why it is not always possible to identify the element.

7. You also stated that many of the legislative proposals would impose far more requirements on what must be included in a letter than what is necessary in the normal course of business to inform the recipient of the patent owner's concerns. What is normal in these kinds of communications today?

Answer: As shown in the letter reproduced in response to question 1, it could be to alert the recipient that it may be engaging in behavior that it previously agreed to avoid and that the sender wishes to discuss the matter. Or it could be, as in the email reproduced in response to question 1, to simply alert a competitor that it may be developing products in a field where the sender has a patent portfolio that the competitor would want to know about before expending significant resources.

8. You stated that patent owners should not be forced to provide burdensome requirements in letters. Is it possible to prevent patent trolls from preying on small businesses by eliminating the vagueness of their abusive letters without disclosure requirements?

Answer: Yes. By placing the emphasis on eliminating false and fraudulent statements contained in bad faith patent demand letters, rather than by enumerating a list of specific requirements for all patent enforcement or demand letters. Requiring information to be included in a patent enforcement letter that has no bearing on whether the entity is sending a bad faith patent demand letter containing false and fraudulent statements would burden patent holders acting in good faith and should be avoided.

9. At the time of our hearing, there were at least five State laws regarding the contents of a patent demand letter, with another two bills awaiting a Governor's signature. In addition, there were bills pending before somewhere around 19 State legislatures. If we move forward with Federal legislation on this matter but do not include preemption, what would be end result?

Answer: We would have a hodgepodge of conflicting laws in the states regulating behavior that would impact a national system of patents. This would be bad for the patent system and innovators using the patent system. The right to create a national patent system was exclusively given to the Congress in Article 1 of the Constitution for a reason – to ensure a uniform practice throughout the country. Allowing 50 different legislatures to enact laws impacting patent rights would upset this Constitutionally mandated uniformity, create extra burdens and costs on users, and dilute the patent system's incentives to create and develop innovative new technologies. In short, the end result would be fewer communications.

The Honorable Jan Schakowsky

1. Some state and federal legislative proposals to address abusive patent demand letters include provisions specifying exactly what information such letters must include. A list of commonly suggested requirements is below. Please provide the Subcommittee with your written views on whether patent demand letters should include:

Before addressing each of the specific "commonly suggested requirements" set forth in this question, let's say that some of them may be appropriate to include in some demand letters. For example, often it may be appropriate to include the patent number, the owner of the patent and the parent company, if any, of the patent owner. On the other hand, some of the "commonly suggested requirements" in this question go beyond what is needed to put the recipient on fair notice of the nature or purpose of the communication and are unduly burdensome for patent owners. Such overly-burdensome requirements include, for example, a "description of each claim of the patent being infringed." Often the information needed to identify each claim of the patent believed to be infringed is solely within the control of the recipient, and imposing such a requirement on the patent holder, at the risk of being charged with sending a bad-faith demand letter if it is not included, would be unfair to patent owners and would curtail legitimate patent licensing and enforcement communications.

Even for the "commonly suggested requirements" that may be appropriate in the case of some demand letters, they may not be appropriate for all letters. A list of the patent numbers the sender may believe are being infringed, for example, may not be appropriate to require in each demand letter. In the case of legitimate business-to-business letters, often an initial communication from the patent owner may be designed to offer a license to an entire patent

portfolio, in which case the specific patent numbers may be provided in later communications once the parties have entered into a nondisclosure agreement. Indeed, under current patent law, the patent owner should not be required in all cases to include the patent number in an initial communication, because it may subject the patent owner to the risk that the recipient may file a declaratory judgment action against the patent owner in a venue unfavorable to the patent owner. As a result, the initial communication may invite the recipient to enter into a nondisclosure and standstill agreement, under which the parties may then exchange detailed information about the patents under consideration and the recipient's products, processes or business interests. Requiring each demand letter to include a list of the patent numbers the sender may believe are being infringed would disrupt this process and impede these legitimate types of patent communications.

To be clear, bad-faith demand letters are a problem and we strongly support finding a fair and effective solution to end them. At the same time, however, legislation in this area must reflect the balance necessary to ensure that efforts to address patent demand letter abuses do not inadvertently chill the legitimate patent communications patent owners engage in each and every day. The patent system is designed to encourage notice and communication of patent rights as an efficient way to resolve infringement disputes short of filing lawsuits, as well as to promote the licensing and dissemination of new technologies. There is a distinct and critically important difference between those who send false and misleading demand letters to small businesses, retailers and banks and the vast majority of patent holders, including individual inventors and universities, who legitimately send notices to alert the public of their patent portfolios, to offer them for license and, when necessary, to prevent their patented products from being infringed.

The key to legislation that appropriately recognizes this distinction and targets abusive demand letters, while not chilling legitimate patent licensing and enforcement communications, is to identify a basic set of information typically appropriate to be included in patent demand letters that fairly balances the recipient's need for information against the burden and risk to the patent owner of providing such information. The legislation should provide authority to bring enforcement actions against those who send letters that do not contain such information only when the information is omitted in bad faith, i.e., the information is omitted to mislead or deceive the recipient. This approach protects legitimate patent communications and appropriately targets enforcement authority to those who need protection against bad-faith demand letters. The enforcement resources of the FTC and state Attorneys General are finite and should not be called upon to aid recipients of legitimate patent licensing communications, or companies that are fully capable of defending themselves against demand letters. It also ensures that the legislation is narrowly-tailored to mitigate First Amendment concerns associated with the regulation of demand letters, which courts have held are subject to the constitutional protections afforded to petitioning the government for redress.

In the following sections, we explain in more detail our views on the list of "commonly suggested requirements" for patent demand letters.

- a. Description of each patent being infringed, including patent number;

The patent system is designed to encourage notice and communication of patent rights as an efficient way to resolve infringement disputes short of filing lawsuits, as well as to promote the licensing and dissemination of new technologies. Those activities comprise the vast majority of letters sent to notify the recipients of the existence of patent rights. There is a distinct and critically important difference between such "patent enforcement letters" and the bad faith patent demand letters containing false and misleading statements sent to hundreds of small businesses, retailers and banks. Unlike the few opportunistic patent assertion entities that send bad faith patent demand letters to extort settlements from innocent end users, the vast majority of patent holders, including individual inventors and universities, legitimately send notices to alert the public of their patent portfolios, to offer them for license and, when necessary, to prevent their patented products from being infringed. While it is desirable to identify the patent being infringed in a patent enforcement letter, there are reasons and situations where it would be appropriate, indeed, advisable to not include such information in a letter. In order to avoid an infringer or potential licensee from filing a declaratory judgment action, a patent owner may not want to identify a specific patent in an initial patent enforcement letter. Rather than demand a specific list of requirements for such letters to contain, it would be far better for legislation to focus on question of whether a letter contains false and misleading information that would transform it into a bad faith demand letter that is designed to intimidate or coerce the recipients into extortionist settlements.

- b. Description of each claim of the patent being infringed;

Answer: See 1a above.

- c. Description of the infringing device, method, or service;

Answer: While it is desirable to identify the activity or product that infringes, it may be impossible for a patent owner to know the specific activity used in a method or process by an infringer since the infringer's manufacturing process is kept secret. Further, it is often impossible to separate chemical ingredients in a product or to determine the exact proportions used by an infringer in its secret formulations. Also, in some cases, the patent owner simply may not have access to the infringing product.

- d. Description of how the device, method, or service infringes;

Answer: As stated in question 1c above, it may be impossible for a patent owner to know the specific activity used in a method or process by an infringer since the infringer's manufacturing process is kept secret. Further, it is often impossible to separate chemical ingredients in a product or to determine the exact proportions used by an infringer in its secret formulations. Also, in some cases, the patent owner simply may not have access to the infringing product. Similarly, it may not be possible to reverse engineer a product to learn the exact steps in a method or process of manufacture without specific knowledge of the infringer's formulations or methods. This often requires discovery from the infringer in order to understand and know the details. This is why business-to-business patent enforcement letters may identify a product or a belief about a method used, but

cannot with specificity identify the specific ingredients, parts, or subcombinations in a product or the specific steps of a process.

- e. Identification of the owner of the patent;

Answer: While a patent owner can generally be identified and disclosed in a business-to-business patent enforcement letter (and must be disclosed in any litigation under the Federal Rules of Civil Procedure), the complexity of ownership of patents, and the free transferability of patents, often makes it difficult and expensive to identify all the owners or licensees of a patent, especially in today's complex corporate environments in which many, many subsidiaries are licensed under, or have a partial ownership interest in, a patent and perhaps under terms of confidentiality.

- f. Identification of the parent company, if any, of the patent owner;

Answer: For the reasons expressed in question 1e above, the complexity of ownership of patents, and the free transferability of patents, often makes it difficult and expensive to identify the parent company and all of the licensees of a patent owner, especially in today's complex corporate environments in which many, many subsidiaries are licensed under, or have a partial ownership interest in, a patent.

- g. Identification of the parent company, if any, of the sender of the letter.

Answer: Since letters are often written by outside counsel, identification of their "parent company" would only reveal the law firm for which they work.

- h. Address of the patent owner and, if a business, also the place of incorporation, principal place of business, and principal business address within the recipient's state;

Answer: For the reasons given in response to question 1e above, it could be difficult and expensive to identify and provide the addresses all the owners or licensees of a patent, especially in today's complex corporate environments in which many, many subsidiaries are licensed under, or have a partial ownership interest in, a patent and perhaps under terms of confidentiality.

- i. Address of the sender of the letter and address of the parent company of the sender of the letter;

Answer: Generally, yes. The address of the sender of the letter writer as well as the role he or she plays can almost always be identified from the letterhead, salutation, or body of the letter. Letters are often written by outside counsel on their letterhead.

- j. Contact information for a person who can discuss resolution;

Answer: Again, generally, yes. The address and name of the sender of a letter will be present and provides a point of contact.

- k. Identification of persons other than the patent owner who may benefit from enforcement;

Answer: See the response to question 6e above.

- l. Identification of any person with the right to enforce each patent;

Answer: See the response to question 6e above.

- m. Identification of all persons that have been granted a license to the patent;

Answer: See the response to question 6e above.

- n. Notice to the recipient that he or she may have the right to have the manufacturer defend the case; and

Answer: Generally, yes.

- o. Some factual basis for the licensing fee or settlement amount demanded.

Answer: The determination of "bad faith" on the basis of subjective factors, such as whether the amount proposed for a license is "reasonable" would lack the objectivity and certainty needed to qualify the sending of such a communication as an unfair or deceptive act.

The Honorable Peter Welch

At the Subcommittee hearing on April 8, 2014, I asked the following question, but there was no time remaining for a response. Therefore, please answer in writing: what evidence do we have about the effect of patent trolls on suppressing innovation?

Answer: We are fortunate to live in the most innovative economy the world has ever seen. We must never take that for granted. Whether by an independent inventor, a university, or a company, the decision to invest the time and resources in the R&D that is needed to make inventions and bring them to market is always a risky proposition. The costs can be high, success uncertain, and any payoff, if it comes at all, may be years away.

Patents help make these investments happen. They provide the legal protection inventors need in order to have a chance to obtain a fair return on what is often years of time, effort and money needed to create inventions and to bring them to the marketplace. Patents provide a secure legal foundation upon which innovators safely can make the investments in research, development, manufacturing and jobs that turn an invention into a business.

A strong patent system is essential to America's ability to compete in markets around the world, America's economic growth, and American jobs. For this reason, innovation protected by strong patent rights is key to our nation's economic growth and the creation of American jobs. According to a study by the U.S. Department of Commerce, intellectual property (IP)-intensive industries support at least 40 million jobs and contribute more than \$5 trillion dollars to the

nation's GDP. On a percentage basis, IP-intensive industries account for more than 27% of the jobs in this country, more than 34% of our GDP and more than 60% of our merchandise exports. It is hardly an overstatement to say that the future of the U.S. economy and our ability to compete successfully in the global economy is dependent on a strong patent system that provides incentives for inventors, universities and companies to invest in the R&D needed to bring innovation to life. Our American innovation engine is the envy of the world, and when considering changes to the patent system that for over 200 years has helped to foster it, our guiding principle should be, first and foremost to "do no harm."

To be clear, bad-faith demand letters, sent by any patent owner seeking to coerce settlements from alleged infringers to avoid the disruption and staggering costs of litigation, have no place in a strong and well-functioning patent system. Such abuses undoubtedly impose needless costs on our patent system and economy.

Not every patent holder is a patent troll. Not every demand letter is sent in bad faith. And not every infringement allegation is unfounded. Far too often, patent enforcement is the only way an American innovator or manufacturer can prevent infringers from free-riding on its R&D investments or can stop infringing knock-offs from threatening to destroy its business. Drafting legislation based on the premise that every patent holder who wishes to enforce its rights is a patent troll, or based on the rhetoric that the patent system is somehow "broken," weakens all patents, favors business models that do not rely on innovation, and tilts the balance in favor of patent infringers, thereby discouraging investments in R&D and innovation.

If the U.S. patent system is weakened, the ensuing damage to American innovation will be difficult, if not impossible, to reverse. For that reason, we need thoughtful, measured and data-driven leadership on this issue that is so vital to American competitiveness, and we urge continued caution and restraint before making changes to a patent system that is so crucial to American innovation. We support balanced, measured reforms to curb patent demand letter abuses while ensuring that the rights of all patent owners to enforce their patents against infringers are not unduly undermined by unbalanced, overly-broad reactions to abuses by some patent owners.

We will know we have the right bill when it garners widespread stakeholder support across industries, and from patent owners and demand letter recipients alike. The bill cannot pick winners and losers among different industries, business models or stakeholder groups. Specifically, what that means is that the bill must reflect a thoughtful balance of interests to:

- Target "bad faith" demand letters, to protect the legitimate licensing and enforcement communications of patent owners and to preserve their First Amendment rights;*
- Focus on the widespread pattern or practice of sending bad faith demand letters, to further the consumer protection roles entrusted to the Federal Trade Commission ("FTC") and state Attorneys General, while not potentially intruding on every individual patent licensing negotiation between a patent owner and a potential licensee;*
- Establish nationwide uniformity in the laws governing patent demand letters that respects the authorities and appropriate roles of the FTC and state Attorneys General; and*

- *Recognize that the enforcement resources of the FTC and state Attorneys General to protect recipients of demand letters are finite and should therefore only be invoked where necessary to further their consumer protection roles.*

FRED UPTON, MICHIGAN
CHAIRMAN

HENRY A. WAXMAN, CALIFORNIA
RANKING MEMBER

ONE HUNDRED THIRTEENTH CONGRESS
Congress of the United States
House of Representatives
COMMITTEE ON ENERGY AND COMMERCE
2125 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6115
Majority (202) 225-2927
Minority (202) 225-3641

June 5, 2014

Mr. Jason M. Schultz
Associate Professor of Clinical Law
New York University School of Law
245 Sullivan Street, Suite 609
New York, NY 10012

Dear Mr. Schultz,

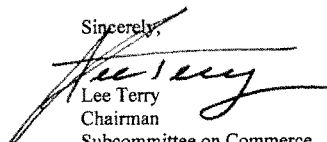
Thank you for appearing before the Subcommittee on Commerce, Manufacturing, and Trade on Tuesday, April 8, 2014 to testify at the hearing entitled "Trolling for a Solution: Ending Abusive Patent Demand Letters."

Pursuant to the Rules of the Committee on Energy and Commerce, the hearing record remains open for ten business days to permit Members to submit additional questions for the record, which are attached. The format of your responses to these questions should be as follows: (1) the name of the Member whose question you are addressing, (2) the complete text of the question you are addressing in bold, and (3) your answer to that question in plain text.

To facilitate the printing of the hearing record, please respond to these questions by the close of business on Thursday, June 19, 2014. Your responses should be e-mailed to the Legislative Clerk in Word format at Kirby.Howard@mail.house.gov and mailed to Kirby Howard, Legislative Clerk, Committee on Energy and Commerce, 2125 Rayburn House Office Building, Washington, D.C. 20515.

Thank you again for your time and effort preparing and delivering testimony before the Subcommittee.

Sincerely,



Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing, and Trade

cc: Jan Schakowsky, Ranking Member, Subcommittee on Commerce, Manufacturing, and Trade
Attachment



New York University

A private university in the public service

School of Law
Faculty of Law

245 Sullivan Street, Room 609
New York, New York 10012-1301
Telephone: (212) 992-7365
E-mail: jason.schultz@nyu.edu

Jason Schultz

*Associate Professor of Clinical Law
Director, Technology Law & Policy Clinic*

June 11, 2014

Dear Chairman Terry, Ranking Member Schakowsky, and members of the Subcommittee,

Thank you for the opportunity to provide answers to questions following up on the April 8, 2014 hearing entitled "*Trolling for a solution: Ending Abusive Patent Demand Letters*". Below are my responses. If I can provide any additional information that might be useful to your proceedings, please do not hesitate to contact me.

Best,

Jason Schultz
NYU School of Law

Additional Questions for the RecordThe Honorable Lee Terry

1. **You testified that in the patent marketplace, companies tend to watch their competitors and competing products very closely so that they can almost always describe how the product or service infringes a patent. Is this always true, particularly in the high-tech industry where you have 1,000 or more patents on a smartphone?**

Answer: Yes. While it is often difficult to map your product to thousands of competitors' patents, it is much easier to map your patents to an individual competitor's particular product. Unlike obtuse patent legalese, product advertising, marketing, and sales descriptions are targeted at customers and thus, must be easier to understand. Moreover, one's own engineers are often experts in the field and are in the best position to assess whether a particular device or service infringes a particular claim of one's portfolio. It is also worth noting that this analysis would only apply to the specific patent claims that one intends to accuse another of infringing in a written letter. It is hard to imagine how one could make sure accusations in good faith without at least some elementary level of analysis of the accused product or service.

For example, at the hearing, Mr. Skarvan expressed concern that requiring analysis of competitor's products before sending a demand letter might inhibit business communications between Caterpillar and its competitors. However, the example he gave involved Caterpillar employees attending a trade show and noticing a new product that might infringe one of Caterpillar's patents. This is exactly the type of situation where Caterpillar should be able to gather any marketing or publicly available technical information it needs to analyze any potential infringement before sending a letter to a competitor. If nothing from the trade show supports an infringement allegation, then one could not send a demand letter in good faith.

2. **Is it always feasible to list the specific patent numbers and claims, even when there may be over 1,000 patents on one high-tech device? If not, what would be a sufficient alternative to listing each and every patent in a situation where you may not necessarily know – you merely suspect – that your IP rights are being infringed? Listing at least just one?**

Answer: I don't believe you have to list every single patent number or claim in every letter – you just have to list the ones that you have a good faith belief are being infringed. If you have over 1,000 patents, it would be bad faith to assert that a high-tech device infringed all of them without going through the proper analysis – doing your homework – and verifying which claims are actually infringed. Sending a demand letter on 1,000 patents without any analysis puts the burden on the defendant to prove a negative – that they don't infringe. That's far more costly, inefficient, and burdensome, especially if the patent language is obtuse or unfamiliar to the defendant. The patentee is in the best position to understand the

patent and its claims and thus, should be required to at a minimum articulate which patents and claims are infringed when accusing another entity of such a serious violation of law.

Moreover, there is no limit on the number of demand letters one can send. So if a company has over 1,000 patents, they could identify the ten most important patents and representative claims within those patents for inclusion in a preliminary letter. This does not preclude them from amending the letter with additional patents or claims at a later date, or sending a second letter when further infringed claims are identified. It just requires that the information in the letter is based on a good faith effort to identify specific instances of infringement. Again, the purpose of any legislation should be to encourage disclosure of information that can help potential defendants evaluate their risks, responsibilities, and options, whether those be to license the patents or to contest the claims in court. Letters that do not include specifics only stir the pot and increase frustration with our patent system; they do not help facilitate licensing and other positive business activities.

The Honorable Jan Schakowsky

1. **Some state and federal legislative proposals to address abusive patent demand letters include provisions specifying exactly what information such letters must include. A list of commonly suggested requirements is below. Please provide the Subcommittee with your written views on whether patent demand letters should include:**
 - a. Description of each patent being infringed, including patent number;
 - b. Description of each claim of the patent being infringed;
 - c. Description of the infringing device, method, or service;
 - d. Description of how the device, method, or service infringes;
 - e. Identification of the owner of the patent;
 - f. Identification of the parent company, if any, of the patent owner;
 - g. Identification of the parent company, if any, of the sender of the letter;
 - h. Address of the patent owner and, if a business, also the place of incorporation, principal place of business, and principal business address within the recipient's state;
 - i. Address of the sender of the letter and address of the parent company of the sender of the letter;
 - j. Contact information for a person who can discuss resolution;
 - k. Identification of persons other than the patent owner who may benefit from enforcement;
 - l. Identification of any person with the right to enforce each patent;
 - m. Identification of all persons that have been granted a license to the patent;
 - n. Notice to the recipient that he or she may have the right to have the manufacturer defend the case; and
 - o. Some factual basis for the licensing fee or settlement amount demanded.

Responses of Professor Jason Schultz to Questions about Abusive Patent Demand Letters

Answer: I am supportive of including requirements (a)-(l) with two caveats, and of including requirements (m)-(o) with some suggested modifications.

Regarding requirements (a)-(l), for legitimate patentees, this information should be available at low cost. For bottom-feeding assertion entities, it comes at a high cost that breaks their business model. This is exactly the distinction that appropriate legislation should strive to achieve.

Two caveats for requirements (a)-(l): (1) for the descriptions of infringing devices, methods, or services, you might consider making the standard “reasonable” and only requiring that it be based on information available to the patentee at the time the letter is sent, such as from public advertising, marketing, or purchase of the device, method, or service; and (2) parent companies are only one form of obscuring real parties-in-interest when it comes to patent litigation, so it might be worth considering expanding items (f) and (g) to include anyone authorizing the sending of the letter or assertion of the patent against the recipient.

For requirements (m)-(o), this information can be extremely useful for efficiently resolving the dispute outlined in the letter, but I would want to make sure it was only required if the sender (or anyone authorizing the sender) had it within their possession, custody, or control. Otherwise, in some cases, it could be somewhat costly to collect.

2. **Recently, we have witnessed a spate of vague and misleading patent demand letters being sent that fail to provide recipients with even the bare minimum amount of information. These letters are sent indiscriminately to extract settlements, sometimes even from innocent end-users of basic, off-the-shelf electronic equipment.**

This behavior is extremely troubling. I would like to find out how to put an end to this behavior, and how potential legislative fixes should take into account both the rights of legitimate patent holders and the need to clamp down on abusive practices.

- a. **In testimony you submitted for the Subcommittee hearing on April 8, 2014, you wrote that patent owners need to do their “homework” before sending a demand letter. Of course, a lot of work needs to be done both before bringing a lawsuit and during litigation, but what kind of homework should patent owners do to analyze an allegedly infringing product or service before sending a demand letter?**

Requirements (a)-(l) in your first question are an excellent start. The key is to make sure that accusations are individualized for each letter’s recipient and not cookie-cutter or generic. Generic accusations allow bottom-feeding assertion entities to profit from sending multitudes of abusive demand letters. Requirements (a)-(l) do not require anywhere near the same level of homework as filing a lawsuit and, if based only on information available to the sender of the letter at the time it is sent, should not be unreasonably burdensome. But letter senders must be specific enough to include some description that is particular to the recipient and

allows the recipient to evaluate the accusation fairly. This includes information on the patent and real parties-in-interest, which often help recipients identify attorneys who have previous experience with the parties or patents at issue and who could provide useful advice on how to respond to the letter.

b. What are the worst examples you have seen of patent owners asserting claims without conducting any due diligence?

Answer: Project Paperless (<http://arstechnica.com/tech-policy/2013/01/patent-trolls-want-1000-for-using-scanners/>) is a great example of how easy it is to send abusive demand letters without doing any homework. While the letter displayed with the article does identify specific patents by name and number, it provides no information on how the recipient infringes. In fact, it simply states that the recipient “likely [has] an infringing system[.]”

Moreover, even the “generalized” examples of allegedly infringing systems in the letter are immediately disclaimed by the sender as “for your convenience and should not be considered exact substitutes for the more detailed claims.” Of course, no specific detailed claim is identified in the letter as actually being infringed; rather, the letter only identifies “illustrative example” claims and asks the recipient to consider each claim in all of the patents separately. Finally, the letter admits that it has no specific information on the recipient but instead asserts that infringement is likely based on “several marketplace trends and surveys”. This type of generic threatening-yet-vague language is exactly what allows bottom-feeding assertion entities to exist. They can simply copy-and-paste the text from letter to letter and accuse anyone in the world of violating their patents without having to do any specific analysis. Requiring them to do individualized analysis breaks this model.

c. Would the transaction costs of this homework place a burden on legitimate claimants, particularly independent inventors and start-ups? Or is the cost in terms of time and resources reasonable and typical for a company that corresponds regarding patents as part of its routine business practices?

Answer: The transaction costs of this homework would almost certainly be reasonable, especially for independent inventors and start-ups. Independent inventors are likely to only have a few patents and will be experts on the claims and the technology at issue. They can simply look at each recipient’s device, service, or method and write up a brief description of the theory of infringement in the letter, along with other identifying information as listed above. Most of that information will be the same for every letter except for the accusations of infringement. Those accusations can be brief and should only be required to be based on information available to the sender, not on proprietary information or trade secrets. For companies that correspond regarding patents as part of routine business practices, one can easily imagine low-cost mechanisms that have economies of scale over time, such as including the required information in the first letter and then incorporating that information by reference if further demand letters are sent at a later date.

The Honorable Peter Welch

- 1. At the Subcommittee hearing on April 8, 2014, I asked the following question, but there was no time remaining for a response. Therefore, please answer in writing: what evidence do we have about the effect of patent trolls on suppressing innovation?**

Answer: The effect of patent trolls on innovation is complex and multi-faceted, but there are several important studies that make a strong case for the cost these entities impose on legitimate companies and the ways in which they are forcing innovators to divert funds away from R&D to cover the expenses of patent defense. Some of these studies include:

- Lex Machina, 2013 Patent Litigation Review (May 13, 2014), available at <https://lexmachina.com/2014/05/patent-litigation-review/>.
- Smeets, Roger, *Does Patent Litigation Reduce Corporate R&D? An Analysis of US Public Firms* (April 28, 2014). Available at <http://ssrn.com/abstract=2443048> or <http://dx.doi.org/10.2139/ssrn.2443048>
- Bessen, James E. and Meurer, Michael J., *The Direct Costs from NPE Disputes* (June 28, 2012). Cornell Law Review, Vol. 99, 2014, Forthcoming ; Boston Univ. School of Law, Law and Economics Research Paper No. 12-34. Available at <http://ssrn.com/abstract=2091210> or <http://dx.doi.org/10.2139/ssrn.2091210>
- Bessen, James E. and Ford, Jennifer Laurissa and Meurer, Michael J., *The Private and Social Costs of Patent Trolls* (January 9, 2012). Regulation, Vol. 34, No. 4, p. 26, Winter 2011-2012. Available at SSRN: <http://ssrn.com/abstract=1982139>

FRED UPTON, MICHIGAN
CHAIRMAN

HENRY A. WAXMAN, CALIFORNIA
RANKING MEMBER

ONE HUNDRED THIRTEENTH CONGRESS
Congress of the United States
House of Representatives
COMMITTEE ON ENERGY AND COMMERCE
2125 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6115
Majority (202) 225-2927
Minority (202) 225-3641

June 5, 2014

Mr. Mark Chandler
Senior Vice President
And Chief Compliance Officer
Cisco Systems Incorporated
North Building, 9th Floor
601 Pennsylvania Avenue, N.W.
Washington, D.C. 20004

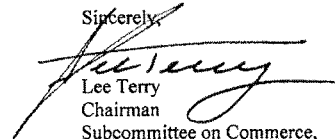
Dear Mr. Chandler,

Thank you for appearing before the Subcommittee on Commerce, Manufacturing, and Trade on Tuesday, April 8, 2014 to testify at the hearing entitled "Trolling for a Solution: Ending Abusive Patent Demand Letters."

Pursuant to the Rules of the Committee on Energy and Commerce, the hearing record remains open for ten business days to permit Members to submit additional questions for the record, which are attached. The format of your responses to these questions should be as follows: (1) the name of the Member whose question you are addressing, (2) the complete text of the question you are addressing in bold, and (3) your answer to that question in plain text.

To facilitate the printing of the hearing record, please respond to these questions by the close of business on Thursday, June 19, 2014. Your responses should be e-mailed to the Legislative Clerk in Word format at Kirby.Howard@mail.house.gov and mailed to Kirby Howard, Legislative Clerk, Committee on Energy and Commerce, 2125 Rayburn House Office Building, Washington, D.C. 20515.

Thank you again for your time and effort preparing and delivering testimony before the Subcommittee.

Sincerely,

Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing, and Trade

cc: Jan Schakowsky, Ranking Member, Subcommittee on Commerce, Manufacturing, and Trade
Attachment

RESPONSE TO ADDITIONAL QUESTIONS FOR THE RECORD

MARK CHANDLER, CISCO SYSTEMS

June 19, 2014

The Honorable Lee Terry

1. **You recommend that a sender of a demand letter be required to include the manufacturer and model number of the allegedly infringing product. Mr. Skarvan gave an example of a situation where his company would not have access to a competitor's manufacturing facility or mine where machinery is located. In that situation, is it reasonable to still require such details for demand letters?**

We understand that some information about an accused product may not be publicly available. However, it is fair to require that the sender of a demand letter make a reasonable inquiry into its basis for alleging infringement (and thus the need for a license), and disclose all the relevant information the sender has about the purportedly infringing product based on that reasonable inquiry. When the sender embarks on a massive campaign to send out hundreds or thousands of demand letters regarding publicly available, mass-produced products, the sender of those letters should provide a list of the products that it believes infringe its patents.

2. **You also recommend that senders of demand letters be required to include a list of all previous licensees so that end users can determine whether the product or service they use is potentially covered by an existing license. Is that something easily done by patent holders?**
 - a. **Are license agreements ever subject to a nondisclosure agreement (NDA) or any other kind of requirement that would preclude a demand letter sender from revealing such information?**
 - b. **Would the name of a patent owner ever be subject to a NDA that would preclude revealing that information in a demand letter?**

In our experience, although the terms of a license may sometimes be confidential, the mere fact of a license is typically not. And even the terms are often disclosable as long as a confidentiality agreement is put in place. It is perfectly reasonable to expect an asserter to disclose the names of existing licensees where that information is non-confidential. If for some reason the identity of a licensee has been made confidential, then the asserter should say that there are licensees whose identity cannot be disclosed and offer to share that information under appropriate confidentiality restrictions. Additionally, the identity of the patent owner should be disclosed; there is no reason to conceal that information.

3. **You state Innovatio is only one example of a growing consumer fraud. You also list MPHJ, Helferich and USEI. Are there other examples? Why do you say it's a consumer fraud rather than a patent dispute?**

We strongly suspect there are others but unfortunately the implicit and even explicit intimidation techniques employed in these letters prevent many of the victims from stepping forward. Although we know that tens of thousands of businesses have been threatened, we need disinfecting sunlight to illuminate the full scope of the problem.

This kind of behavior is fraud because the perpetrators are extorting money based on deceptive and misleading information. The fact that the deception is about the value of patents doesn't make it any less fraudulent than deceptions about bank credit or used cars. Therefore it is fraud when a company demands a hospital or coffee shop either pay it a few thousand dollars for a Wi-Fi device or face an expensive lawsuit, without telling the recipient that the device may already be licensed, that the Wi-Fi chip in the device is worth only a few dollars, or that the license must be reasonable and non-discriminatory.

4. **You stated Helferich demanded licenses of end users that in fact were not required. Is that type of false claim actionable by the victim under current law?**

Cisco has asked the courts to address deceptive practices by filing RICO anti-racketeering claims in its case against Innovatio for, among other things, failing to tell recipients that their products may already be licensed. However, the court dismissed Cisco's claims under the current law, highlighting the need for Congressional action to address this issue.

5. **You also recommend including whether there is a relevant licensing commitment to a standards organization. Can you explain why this is important?**

Companies that want their technology designed into an industry standard must promise to license it to all comers on reasonable and non-discriminatory (RAND) terms or even for free. The patent owner should know whether they or a previous owner made this commitment, since that obligation survives any transfer of the patent to a new owner. Whether or not such a commitment exists is highly relevant to the proper value of a license. It is unfair to leave the demand letter recipient to ferret out this information for himself, assuming he would even know how to look for it.

5. **In a patent rights assertion letter, is it always possible to identify:**

- a. The patent being infringed?
- b. The activity or product that allegedly infringes on the asserted patent?
- c. How the activity or product specifically infringes the asserted patent?
- d. Identify the patent owner?
- e. Identify the letter writer's role?
- f. Provide a point of contact?

If the answer to any of these questions is no, please explain why it is not always possible to identify the element.

a - c

This is all information that is needed to assess the value of the license that is being offered, and in fact necessary to pursue litigation in the event a license is not entered into. The sender of the demand letter is required to conduct this investigation before asserting claims of patent

infringement against an alleged infringer. While there may be specific details of c (how an accused product specifically infringes an asserted patent) that are not publicly available, there should still be a requirement to disclose all of the relevant information available from the sender's reasonable inquiry.

d-f

Yes, the patent owner, point of contact, and the role of the letter writer can and should always be provided. There is no reason to be opaque about who is asserting a patent.

The Honorable Jan Schakowsky

1. Some state and federal legislative proposals to address abusive patent demand letters include provisions specifying exactly what information such letters must include. A list of commonly suggested requirements is below. Please provide the Subcommittee with your written views on whether patent demand letters should include:
 - a. Description of each patent being infringed, including patent number;
 - b. Description of each claim of the patent being infringed;
 - c. Description of the infringing device, method, or service;
 - d. Description of how the device, method, or service infringes;
 - e. Identification of the owner of the patent;
 - f. Identification of the parent company, if any, of the patent owner;
 - g. Identification of the parent company, if any, of the sender of the letter;
 - h. Address of the patent owner and, if a business, also the place of incorporation, principal place of business, and principal business address within the recipient's state;
 - i. Address of the sender of the letter and address of the parent company of the sender of the letter;
 - j. Contact information for a person who can discuss resolution;
 - k. Identification of persons other than the patent owner who may benefit from enforcement;
 - l. Identification of any person with the right to enforce each patent;
 - m. Identification of all persons that have been granted a license to the patent;
 - n. Notice to the recipient that he or she may have the right to have the manufacturer defend the case; and
 - o. Some factual basis for the licensing fee or settlement amount demanded.

All of these items should be included in the demand letter. The recipient needs to know a-d and o to assess the value of a license and whether there is even infringement of a valid patent for which a license is required. It is entirely unreasonable to hide the information the recipient needs to assess the demand letter. The recipient should also know who they are being asked to negotiate with (e-l) and the identity of existing licensees (m). PAEs often create a complicated web of ownership, and a recipient needs to be able to determine whether it already has a license through an agreement with a parent or affiliate, and also whether it is currently negotiating with a related entity. Finally, the recipient should be informed of the possibility that one of their suppliers should be defending them (n).

The Honorable Peter Welch

1. **At the Subcommittee hearing on April 8, 2014, I asked the following question, but there was no time remaining for a response. Therefore, please answer in writing: what evidence do we have about the effect of patent trolls on suppressing innovation?**

Numerous studies now show that PAEs are harming innovation. Professors James Bessen and Michael Meurer of Boston University found that PAEs cost the economy \$29 billion dollars a year (http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2091210) Professor Colleen Chien of Santa Clara University found that small businesses and start-ups make up more than half of the victims of PAE assertions (<http://patentlyo.com/patent/2013/03/chien-patent-trolls.html>). Professor Catherine Tucker of MIT found that the impact of PAE assertions reduced VC funding by at least \$8 B over past 5 years. <http://cdn.arstechnica.net/wp-content/uploads/2014/06/Tucker-Report-5.16.14.pdf>

FRED UPTON, MICHIGAN
CHAIRMAN

HENRY A. WAXMAN, CALIFORNIA
RANKING MEMBER

ONE HUNDRED THIRTEENTH CONGRESS
Congress of the United States
House of Representatives
COMMITTEE ON ENERGY AND COMMERCE
2125 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6115
Majority (202) 225-2927
Minority (202) 225-3641

June 5, 2014

Mr. Michael Dixon, Ph.D.
President and CEO
UNeMed Corporation
University of Nebraska Medical Center
986099 Nebraska Medical Center
Omaha, NE 68198

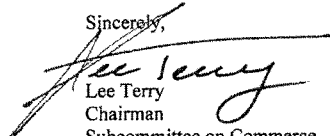
Dear Mr. Dixon,

Thank you for appearing before the Subcommittee on Commerce, Manufacturing, and Trade on Tuesday, April 8, 2014 to testify at the hearing entitled "Trolling for a Solution: Ending Abusive Patent Demand Letters."

Pursuant to the Rules of the Committee on Energy and Commerce, the hearing record remains open for ten business days to permit Members to submit additional questions for the record, which are attached. The format of your responses to these questions should be as follows: (1) the name of the Member whose question you are addressing, (2) the complete text of the question you are addressing in bold, and (3) your answer to that question in plain text.

To facilitate the printing of the hearing record, please respond to these questions by the close of business on Thursday, June 19, 2014. Your responses should be e-mailed to the Legislative Clerk in Word format at Kirby.Howard@mail.house.gov and mailed to Kirby Howard, Legislative Clerk, Committee on Energy and Commerce, 2125 Rayburn House Office Building, Washington, D.C. 20515.

Thank you again for your time and effort preparing and delivering testimony before the Subcommittee.

Sincerely,

Lee Terry
Chairman
Subcommittee on Commerce,
Manufacturing, and Trade

cc: Jan Schakowsky, Ranking Member, Subcommittee on Commerce, Manufacturing, and Trade
Attachment

Responses to questions by
Subcommittee on Commerce, Manufacturing, and Trade
Committee on Energy and Commerce
United States House of Representatives
113th Congress, 2nd Session
April 8, 2014
Michael J. Dixon, Ph.D.
President and CEO, UNeMed

The Honorable Lee Terry

1. You noted that UNeMed and UNMC were able to partner with Boston Scientific to bring the LeVeen Radiofrequency Ablation Probe to market. I want to use this example to talk about how you would assert your rights in a demand letter (not a letter marketing to potential licensees).
 - a. Who owns the right to assert the patent against potential infringers? UNeMed, UNMC, or Boston Scientific?

[Michael Dixon response]: It depends on the license. If it is a nonexclusive license or in a specific field, we often retain the first right to pursue infringers. If we decline, our licensee typically has the right to enforce.

If it is an exclusive license, as was the case with the LeVeen Radiofrequency Ablation Probe, we may allow the commercialization partner (e.g. Boston Scientific) to have the first right to enforce the patent rights at their expense. If they choose not to enforce, we would then have an opportunity to enforce at our own expense.

- b. If the entity with the right to assert the patent found a potentially infringing ablation probe, what would be included in the demand letter?

[Michael Dixon response]: Again it would largely depend on the situation and the license. In the case of an exclusive license that gave Boston Scientific the first right to enforce, they would determine the scope of the infringement and the contents of the demand letter. The letter may identify 1) the intellectual

property (and possibly the claim or claims) that is being infringed; 2) the product which is infringing the intellectual property; 3) the licensee or owner responsible for enforcing the patent(s); 4) a request that the infringing party either cease and desist or enter into license negotiations; and 5) a point of contact to further discuss final resolution of the matter. This type of communication is variable depending on the situation and not taken lightly as the first communication is often sent in an effort to prevent litigation (e.g. to avoid provoking a Declaratory Judgment suit).

- c. Are there any circumstances where one of the entities [UNMC, UNeMed, or Boston Scientific – whichever of the two that is not the answer to the first question above] that don't have the right to assert the patent would want to send a demand letter?

[Michael Dixon response]: In almost all licensing situations, one party has the first right to enforce the patent – but if they don't (often within a specific amount of time), the other party has the option to enforce at their own expense. The party with the first right to enforce takes precedence and generally is not superseded by the secondary party with a right to enforce until the specific time period has elapsed.

2. You stated that two types of communications could be considered demand letters: marketing inventions for investment and letters alleging infringement. Could you please explain how a solicitation letter could be considered a demand letter? How could a communication offering a license to an invention to someone who does not currently utilize that invention be confused with a communication alleging infringement?

[Michael Dixon response]: Marketing letters, or more broadly, “business communication letters” may identify intellectual property (IP) that the sender believes a company would be interested in licensing and/or developing. For us, business communication letters are usually written in general terms and describe our innovation and its potential contribution to the marketplace. For example: “We noticed that you are interested in developing cancer vaccines, we thought you might be interested in looking at a new vaccine developed at UNMC. Here are some details on our new vaccine technology... Please let us know if you would be interested in discussing a license”.

I haven't seen a specific definition of a “Demand Letter”, but in my opinion, it would be a letter that specifically states an infringement lawsuit will be filed if the recipient doesn't comply with the demands of the letter (e.g. licensing or cease and desist activity).

While a letter offering a license to an invention may be vague, it is often going to a company that is working in the same field as our innovation. Therefore, it is possible for that company to view a marketing letter as a threat (especially if they have an internal, unpublished innovation that is very similar to our IP). If they have products in the pipeline that are similar, even though we lack sufficient detail to know what the company is developing, our marketing letter may be viewed as putting them on notice of our IP rights.

3. You listed the elements you believe could be disclosed in a demand letter that would not upset the balance needed to protect your rights as a patent holder. Are there additional disclosures that could be included in legislation that would not upset the balance?

[Michael Dixon response]: At this time I cannot think of any additional elements that would be essential. Overall, I believe it's important to only require the minimal amount of information that will allow the party receiving the letter to react in an informed manner. Requiring more than these essential elements has the potential to adversely affect legitimate patent rights assertion letters.

4. In a patent rights assertion letter, is it always possible to identify:
 - a. The patent being infringed?
 - b. The activity or product that allegedly infringes on the asserted patent?
 - c. How the activity or product specifically infringes the asserted patent?
 - d. Identify the patent owner?
 - e. Identify the letter writer's role?
 - f. Provide a point of contact?

If the answer to any of these questions is no, please explain why it is not always possible to identify the element.

[Michael Dixon response]: As I've stated previously, the definition of a patent rights assertion letter may have broad interpretation, so it is difficult to answer any of these questions specifically. In general, if the sender has done their homework (which often means multiple business communication letters prior to sending a patent rights assertion letter), the receiver should be able to answer the questions above in the patent rights assertion letter.

5. Do any of the State laws on demand letters cause you concern? If so, why?

[Michael Dixon response]: While I am not an expert on all of the potential state laws, I do have concerns that some of the proposed state legislation may lead to state courts determining what is a frivolous patent claim and what is not. Patent claim construction is a very esoteric art, and interpretation of patent validity is best handled at the federal level.

6. At the time of our hearing, there were at least five State laws regarding the contents of a patent demand letter, with another two bills awaiting a Governor's signature. In addition, there were bills pending before somewhere around 19 State legislatures. If we move forward with Federal legislation on this matter but do not include preemption, what would be end result?

[Michael Dixon response]: As I stated above, my concern if federal law doesn't preempt state laws is that we will end up with a patchwork of laws that makes it burdensome for legitimate patent enforcement – which is essential for our innovation ecosystem. Companies that rely on patents are not only national, but often international. It is important to give them a legal structure that allows them to 1) understand what is required, and 2) operate within that legal structure effectively.

The Honorable Jan Schakowsky

1. Some state and federal legislative proposals to address abusive patent demand letters include provisions specifying exactly what information such letters must include. A list of commonly suggested requirements is below. Please provide the Subcommittee with your written views on whether patent demand letters should include:
 - a. Description of each patent being infringed, including patent number;
 - b. Description of each claim of the patent being infringed;
 - c. Description of the infringing device, method, or service;
 - d. Description of how the device, method, or service infringes;
 - e. Identification of the owner of the patent;
 - f. Identification of the parent company, if any, of the patent owner;
 - g. Identification of the parent company, if any, of the sender of the letter;
 - h. Address of the patent owner and, if a business, also the place of incorporation, principal place of business, and principal business address within the recipient's state;
 - i. Address of the sender of the letter and address of the parent company of the sender of the letter;
 - j. Contact information for a person who can discuss resolution;
 - k. Identification of persons other than the patent owner who may benefit from enforcement;
 - l. Identification of any person with the right to enforce each patent;
 - m. Identification of all persons that have been granted a license to the patent;
 - n. Notice to the recipient that he or she may have the right to have the manufacturer defend the case; and
 - o. Some factual basis for the licensing fee or settlement amount demanded.

[Michael Dixon response]: The first question that I believe needs to be answered is “What is a demand letter”? Once that is established, I believe a minimum amount of disclosure is good. We must be careful not to treat all business communications regarding intellectual property as demand letters.

This list is quite extensive and may not be appropriate in every case. In complex infringement cases, it is possible the patent owner may not know all of the inner workings of the infringing technology – that is why business communications highlighting the issued patent and potential infringing technology are necessary. Therefore, in items (a-d) above, it may not be possible to provide a detailed description.

I don’t believe items (k), (l) (m), or (n) are applicable, nor are they practical. For universities, there may be a long list of inventors – and it isn’t practical for our licensees to list our inventors on every patent infringement letter. Furthermore, listing entities which have received a license for IP may not be applicable (or in the worst case, it may actually be misleading). Still further, (n) is not applicable for any biotechnology or life science patent infringement, so requiring it in all demand letters may cause more confusion.

Finally, regarding item (o), it is difficult to determine licensing fee or settlement amounts without knowing the financials of the infringing party. Requiring data based upon so many unknowns at an early stage is not useful.

The Honorable Peter Welch

1. At the Subcommittee hearing on April 8, 2014, I asked the following question, but there was no time remaining for a response. Therefore, please answer in writing: what evidence do we have about the effect of patent trolls on suppressing innovation?

[Michael Dixon response]: Innovative startup companies face many challenges including developing new products, marketing, and creating customers in an often competitive and crowded environment. All of these challenges help separate the wheat from the chaff, allowing the strongest new companies with the best products to succeed. Patent trolls, however, are an unnecessary predator, preying on these companies when they are most vulnerable; when they are often short on resources, but high on promise. Unfortunately, resources for startups are often incredibly thin and the time/money used to fight a patent troll is money not used to develop the company; thus retarding its development and potentially causing it to wither away before it develops further.

One example: One of the companies with whom we work created a novel medical device and invested many years (and dollars) developing it. Just days after they received FDA approval, a patent troll sent them a letter demanding money for a process that is common in every hospital in the nation. Unfortunately, instead of ramping up marketing and sales, and making an innovative product available to the public, the company had to spend precious time and resources researching and dismissing the bogus claim. It is only one example, but this same story repeats across the nation as this patent troll targets small companies immediately after they receive FDA clearance.